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PROPOSALS TO LIBERALIZE THE SOCIAL SECURITY RETIREMENT TEST AND TO REPEAL CERTAIN SOCIAL SECURITY BENEFITS

HEARING

BEFORE THE

SUBCOMMITTEE ON SOCIAL SECURITY

OF THE

COMMITTEE ON WAYS AND MEANS

HOUSE OF REPRESENTATIVES

ONE HUNDRED FIRST CONGRESS

FIRST SESSION

MAY 25, 1989

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PROPOSALS TO LIBERALIZE THE SOCIAL SECURITY RETIREMENT TEST AND TO REPEAL CERTAIN SOCIAL SECURITY BENEFITS

THURSDAY, MAY 25, 1989

HOUSE OF REPRESENTATIVES,
COMMITTEE ON WAYS AND MEANS,
SUBCOMMITTEE ON SOCIAL SECURITY,
Washington, DC.

The subcommittee met, pursuant to notice, at 10:05 a.m., in room 2359-A, Rayburn House Office Building, Hon. Andrew Jacobs, Jr. (chairman of the subcommittee) presiding.

[The press release announcing the hearing follows:]

FOR IMMEDIATE RELEASE
MONDAY, MAY 15, 1989

PR #6
SUBCOMMITTEE ON SOCIAL SECURITY
COMMITTEE ON WAYS AND MEANS
U.S. HOUSE OF REPRESENTATIVES
1102 LONGWORTH HOUSE OFFICE BLDG.
WASHINGTON, D.C. 20515
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ANDREW JACOBS, JR. (D., IND.), CHAIRMAN
SUBCOMMITTEE ON SOCIAL SECURITY,
COMMITTEE ON WAYS AND MEANS, U.S. HOUSE OF REPRESENTATIVES,
ANNOUNCES A HEARING ON
PROPOSALS TO LIBERALIZE THE SOCIAL SECURITY RETIREMENT TEST
AND TO REPEAL CERTAIN SOCIAL SECURITY BENEFITS,
ON THURSDAY, MAY 25, 1989, AT 10:00 A.M.,
IN ROOM 2359-A RAYBURN HOUSE OFFICE BUILDING

Andrew Jacobs, Jr. (D., Ind.), Chairman of the Subcommittee on Social Security, Committee on Ways and Means, U.S. House of Representatives, announced today that the Subcommittee will hold a hearing on liberalizing the social security retirement test and repealing certain social security benefits. The hearing will be held on Thursday, May 25, 1989, in room 2359-A Rayburn House Office Building, beginning at 10:00 A.M.

The social security retirement test determines to what degree a person who is eligible for social security benefits is actually retired and, therefore, entitled to retirement benefits. Currently, individuals age 62-64 may earn up to $6,480 a year in wages or self-employment income and still be treated as retired. The test for people age 65-69 is $8,880 a year. The exempt amounts are adjusted each year to reflect changes in average wages in the economy. For earnings in excess of these amounts, $1 of benefit is lost for each $2 of non-retirement earnings. Beginning in 1990, a beneficiary who is age 65-69 will forfeit only $1 in benefit for every $3 in non-retirement earnings. People age 70 years and older are not subject to the test.

Some proponents of liberalizing the retirement test have proposed raising the figure for 1990 by about $1,000. Others have proposed raising the figure by $3,000 in 1990, by another $3,000 in 1991, and by an additional $3,000 in 1992, and eliminating the limitation entirely by 1995. These proponents have proposed offsetting a portion of the cost of this increase by repealing retroactive benefits for certain individuals eligible for reduced social security benefits. Under current law, some individuals are permitted to receive benefits for up to six months prior to their actual application for social security benefits if eligible for benefits during those six months. The proposal would eliminate this treatment in two categories: 1) those with dependents entitled to unreduced benefits, and 2) those with pre-retirement earnings over the amount allowed under the retirement test.

The cost over five years of liberalizing the retirement test by $1,000 in 1990 is $1.2 billion. The five-year cost of increasing the figure in $3,000 increments is $6.3 billion. The savings resulting from repealing the two categories of social security benefits is $0.8 billion.

The Subcommittee would like to hear witnesses' views on increasing the retirement test. The Subcommittee would also like to hear witnesses' views concerning the proposal to eliminate the two categories of retroactive benefits. The Subcommittee recognizes the constraints of the budget and is concerned about additional expenditures from the social security trust funds. Thus, the Subcommittee would like to hear proposals from each witness on means of financing the full cost of any increase in the retirement test which the witness recommends.

DETAILS FOR SUBMISSION OF REQUESTS TO BE HEARD:

Requests to be heard at the hearing must be made by telephone to Harriett Lawler or Diane Kirkland [(202) 225-1721] by noon Friday, May 19, 1989. In order to facilitate scheduling, requests should indicate the specific issues that the witness wishes to address. The requests should be followed by a formal written request addressed to Robert J. Leonard, Chief Counsel, Committee on Ways and Means, U.S. House of Representatives, 1102 Longworth House Office Building, Washington, D.C. 20515. The Subcommittee will notify by telephone those scheduled to appear as soon as possible after the filing deadline. Any questions regarding a scheduled appearance should be directed to the Subcommittee staff [(202) 225-9263].

In view of the limited time available to hear witnesses, the Subcommittee may not be able to accommodate all requests to be heard. Those persons and organizations not scheduled for an oral appearance are encouraged to submit written statements for the record of the hearing. All persons requesting to be heard, whether they are scheduled for oral testimony or not, will be notified as soon as possible after the filing deadline.

Witnesses scheduled to present oral testimony are required to summarize briefly their written statements in no more than five minutes. THE FIVE-MINUTE RULE WILL BE STRICTLY ENFORCED. Subcommittee Chairman Jacobs advises witnesses that they will be allowed no more than two "finally's" and one "in conclusion." The Congressional Budget Office and similar U.S. Government agencies may be granted an exception. The full written statement of each witness will be included in the printed record.

In order to assure the most productive use of the limited amount of time available to question witnesses, those scheduled to appear before the Subcommittee are required to submit 100 copies of their prepared statements to the Subcommittee on Social Security office, room B-316 Rayburn House Office Building, at least 24 hours in advance of their scheduled appearances. Failure to do so may result in the witness being denied the opportunity to testify in person.

WRITTEN STATEMENT IN LIEU OF PERSONAL APPEARANCE:

Persons submitting written comments for the printed record of the hearing should submit six (6) copies by the close of business, Thursday, June 8, 1989, to Robert J. Leonard, Chief Counsel, Committee on Ways and Means, U.S. House of Representatives, 1102 Longworth House Office Building, Washington, D.C. 20515. If those filing a written statement for the record of the printed hearing wish to have their statements distributed to the press and the interested public at the hearing, they may provide additional copies for this purpose to the Subcommittee, room B-316 Rayburn House Office Building, on the day of the hearing.

FORMATTING REQUIREMENTS:

Each statement presented for printing to the Committee by a witness, any written statement or exhibit submitted for the printed record or any written comments in response to a request for written comments must conform to the guidelines listed below. Any statement or exhibit not in compliance with these guidelines will not be printed, but will be maintained in the Committee files for review and use by the Committee.

1. All statements and any accompanying exhibits for printing must be typed in single space on legal-size paper and may not exceed a total of 10 pages.
2. Copies of whole documents submitted as exhibit material will not be accepted for printing. Instead, exhibit material should be referenced and quoted or paraphrased. All exhibit material not meeting these specifications will be maintained in the Committee files for review and use by the Committee.
3. Statements must contain the name and capacity in which the witness will appear or, for written comments, the name and capacity of the person submitting the statement, as well as any clients or persons, or any organization for whom the witness appears or for whom the statement is submitted.
4. A supplemental sheet must accompany each statement listing the name, full address, a telephone number where the witness or the designated representative may be reached and a topical outline or summary of the comments and recommendations in the full statement. This supplemental sheet will not be included in the printed record.

The above restrictions and limitations apply only to material being submitted for printing. Statements and exhibits or supplementary material submitted solely for distribution to the Members, the press and public during the course of a public hearing, may be submitted in other forms.

Chairman JACOBS. The hearing today of the subcommittee is on the proposal to liberalize the retirement test under Social Security. And our first witness is the Right Honorable William Archer from the empire of Texas.

I tried to stretch it out as long as I could to give you time to finish your conference.

STATEMENT OF HON. BILL ARCHER, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF TEXAS

Mr. ARCHER. Mr. Chairman, I thank you very much.

Since we have the ability to divide into 5 States and have 10 Senators, I guess the term "empire" may still be appropriate.

Chairman JACOBS. That's a mild term.

Mr. ARCHER. Mr. Chairman, thank you so much for calling these hearings today. You have been very generous in doing that. I wish that our full committee could accommodate hearings on some of the items that many of us would like to see, as well as you have on this subcommittee. And I am delighted that you permitted me to be the first witness on a matter that I have had a warm interest in, and that's an understatement, for many, many years, in fact since I first came on this committee.

I realize that you have quite different views than I do on this subject, and I respect those views, as I respect you.

Chairman JACOBS. Well, so far we agree on Texas.

Mr. ARCHER. Yes.

You, I know, sincerely believe that the elimination of the earnings limit would be a boon to the more affluent, and I do not. Under the current law, the affluent are the ones most able to forego the benefits. It is the middle class who really, in my opinion, are being squeezed out of the labor market.

And I have introduced two bills in this Congress dealing with the issue, H.R. 58 and H.R. 2348. H.R. 58 calls for the outright repeal of the earnings limitation for all beneficiaries now affected.

I cannot help but finally remember for the committee that Barry Goldwater was the sponsor of this legislation for each year that he served in the Senate until he retired. And it would be a wonderful memorial to him were we able to enact this.

Among others, H.R. 58 would benefit surviving spouses with minor children, which is another problem, Mr. Chairman. It is not just those who reach retirement age that are affected. I have a daughter in my own family, who is a widow, whose husband died at age 27 and left her with a little baby girl. And she very much wants to work, particularly now that that child is old enough to go into kindergarten. And yet she finds that to work would cause her a loss of her benefits. And the limit is a much lower one, as you know, it's not the $8,880 limit, it's in the $6,000 range. She wants to be independent and earn that money, and it's quite a deterrent to lose benefits when she does.

It seems contrary to program purposes to require that a single parent forego a small benefit by working. I say a small benefit because the family maximum acts as a cap on total benefits. This outright repeal remains my long-term goal but, in the interim, I will support other measures to liberalize the current limit.

Last year, I introduced the Worker's Option Act, phasing out the test by age for workers 65 to 69. This year, my Worker's Option Act, H.R. 2348, calls for the outright repeal at the normal retirement age, now 65. The net 3-year cost would be just under $10 billion, according to Social Security Administration actuaries.

Sadly enough, Mr. Chairman, these estimates do not take into account reflow into the Treasury, as a result of people working. And I think that's sad. As you know, AARP is strongly in support of this legislation because they recognize that it would increase the number of elderly working, and the entire Nation would benefit from that in economic ways which would generate significant additional revenue into the Treasury.

Mr. Chairman, you have asked that we address the issue of how to pay for liberalizing the earnings limit. As our good friend, Robert Myers, the former Chief Actuary for Social Security, recently testified, it isn't a matter of how, it's really a matter of when.

Under current law, we will pay for the elimination of the limit at the point when the delayed retirement credit has reached 8 percent. That is around the year 2008. At that point, from the long-term perspective of the trust funds, the decision to retire or continue working will be a wash.

But, in my view, it isn't a wash when we consider the impact of that retirement decision on the health and income of the worker, or on the national economy. We have so much more to gain by keeping productive workers in the labor force. And I might add that I believe someone who is happily working after the age of 65, and who does so voluntarily is going to be in better health and require less in the way of medical treatment, which is a major savings. Medical treatment is a growing part of the cost of living in this country.

An earnings limit which effectively returns 10 to 20 cents in spendable income for every dollar earned is a profound work disincentive for middle-income workers. We cannot really look at this issue in a vacuum but rather in coordination with the other work deterrents for those 65 and over. They must continue to pay the payroll tax. They have 50 percent of their benefits subject to income tax. And they now must pay an income tax surtax, the highest in the land, in order to pay for catastrophic coverage, not just for themselves, but for everybody else who is covered gratis.

The combination of all of those items gets you to an effective marginal tax rate in some instance of over 100 percent. And that clearly is a great, great deterrent to seeing productivity continue on the part of those who have the experience and the desire to continue to work.

I have advocated repeal of the earnings limit for 18 years, during which time I've watched the ratio of workers to retirees shrink from 3.7 to 3.3. By the time the delayed retirement credit reaches 8 percent and offers workers a fair choice, the ratio will be 3 to 1. Like Atlas, tomorrow's workers will shoulder a growing burden of beneficiaries.

I know, Mr. Chairman, you have got to consider the startup costs. And H.R. 2348 has several offsets you may wish to consider. One is the immediate implementation of the 8 percent delayed retirement credit. Another feature would prohibit retroactive entitlement to reduced benefits, a provision also proposed by Senator Armstrong.

Mr. Chairman, frequently this effort to eliminate the retirement earnings test limit is questioned because of the return that retirees get from Social Security benefits compared to what they paid in during their working years. Admittedly, for those who have retired in previous years who paid in on a major portion of their work life at a 1-percent rate, and a $3,000 wage limit, the amount that they get back is significantly in excess of what they paid in. But now that workers are paying in with a tax over 15 percent of payroll, the amount that they will receive back in the years to come will be less and less in excess of what they paid in during their work lives. And I think that we have got to remember that.

In addition, if that is a valid argument, then in order to be equitable, the Congress would have to look at, for example, say Federal retirement in which retirees receive back an enormous amount in excess of what they paid during their work lives, and say, well, now, if you continue to work, you're going to suffer a reduction in your committed and contracted retirement benefit. I do not urge that. I do not suggest it. I only say that if that argument is an effective one, then we would have to look at every other retirement system in this country, including private retirement plans in order to treat Social Security equitably with them.

Those retroactive reduced benefits that Senator Armstrong talked about as a method of recouping some of the costs of this constitute an unexpected windfall for months before retirement. Any worker who planned to claim such benefits could have done so easily by phone or mail any time after age 62. I think the tradeoff—eliminating a windfall for retroactive months of work in exchange for continued employment after age 65—is a sound one.

Mr. Chairman, the demographic clock is ticking. Our productive work force is aging. And I believe it is time to remove this last vestige of age discrimination embodied in Federal statute.

Thank you so much for permitting me to testify.

Chairman JACOBS. Thank you, Mr. Archer.

As I understand it, the repeal of the retroactive benefits would amount to about $700 million over 5 years, and I infer that that would just about pay for the $1,000 increase next year from $10,000 to $11,000 roughly of permitted earned income while a person is still deemed retired despite earning the $11,000 per year. That's $700 million over 5 years.

We had a hearing 2 days ago about the most elderly Social Security retirees. And the story about them is absolutely stark. It is a stunning story. They're the dog food people. And they are mostly women who are octogenarians and above. Their incomes are from Social Security and SSI. Many of them don't even claim SSI by the way for various reasons according to the hearing. I think it could be characterized as a national disgrace.

So the question occurs on the Armstrong proposal now, not on any part that you were talking about.

If we did repeal the retroactive benefits, which I agree with you are marginal in social worth, would the money better be put to use for those extremely impoverished widows above the age of 80 who, I might add, are presumed not to be so able-bodied or even so capable of looking after their own homes and housekeeping and so forth.

Mr. ARCHER. Well, Mr. Chairman, we, of course, could debate the priority of interest of where to put any amount of money being spent out of the Federal budget.

My interest in the bills that I have presented is to encourage and create an incentive for greater productivity in this country, and greater mental and physical health on the part of the elderly. And I would hope that whatever we did on this would be done in such a way that it would move toward those goals.

If there is a greater need for the purpose of social policy to take care of those who are over 80, which we all of us have a great concern about, then I would think we should have an outreach program under SSI. Concerning those in need who, do not have the financial wherewithal, and perhaps have low Social Security benefits because of lower earnings, that we would look to the SSI program rather than putting the burden on the Social Security program. I would hope we could continue to push the latter as much as possible toward an insurance concept and a matter of earned right rather than a welfare concept.

Chairman JACOBS. According to the figures I've been given, a typical person, whom I referred to a moment ago, would receive something less than $4,000 a year and, in most cases, without any capability of obtaining outside earnings even with SSI payments. That's the magnitude of that problem.

But on the question of incentive, I notice in your testimony you said that many people, I'm persuaded most people, who are capable of doing so work as a good mental health factor.

So the question is, what would happen to the average American who has this good feeling about working, maybe a bad feeling about not working, if he or she just was given the plain choice between the $12,000 a year in Social Security benefit or $12,000 earned income, what do you think that person would choose?

Mr. ARCHER. Well, I'm not sure what they would choose. I think it would depend on each individual. But I will say that again we get back to some of the basic questions of what is the basis of Social Security? Is it to be considered a welfare program or is it to be considered a matter of earned right?

In 1982, during the deliberations of the National Commission on Social Security Reform of which I was privileged to be one of the 15 members, I offered a complete substitute for the Social Security Program which would have related benefits to the amount of money paid in during one's work life. This was to implement work done by Michael Boskin who is now Chairman of the Council of Economic Advisers for the President. He had done extensive work on this. It would have been phased in prospectively and would not have affected any of the current beneficiaries.

But I think it is an appropriate design for us to push for, which is to have Social Security as a matter of earned right, separated from the welfare concept. Then take care of the welfare problems, the types of which you mentioned, which the Nation, of course, has a sensitivity to, out of the general fund under a reformed welfare system.

Chairman JACOBS. Well, Bill, I wasn't really advocating that the choice be made. I am only trying to isolate the concept to the question of incentive. And if, on another planet, you had your choice between $12,000 in Social Security retirement benefits or $12,000 that you went to work every day and earned, and you were a good red-blooded American, which choice would you make?

Mr. ARCHER. Well, I would prefer to work. But, you know, I can't speak for every other American.

Chairman JACOBS. But you wouldn't claim to be much better than any other American in terms of——

Mr. ARCHER. No, I certainly wouldn't. And I think the strength of this country is that we have the freedom of choice and the position that each of us takes should not be in some way denigrated by the position that someone else takes.

Mr. SCHULZE. Mr. Chairman, would you yield on that subject for just a minute?

Chairman JACOBS. I'll yield on anything.

Mr. BROWN. As your counselor, let me advise you not to yield on everything. [Laughter.]

Chairman JACOBS. I didn't say everything. I said anything.

Mr. SCHULZE. Having spent 25 years as a small business man before coming here, I think I can give you an idea what an awful lot of the Americans would do, and that's what they are doing. And that's not daily, but monthly.

I had retired seniors who were on Social Security come into my business and offer to work because they wanted to work, but they asked to be paid under the table. They wanted to be paid in cash and they would work for less. They wanted to be productive.

So it seems to me what we are doing in effect is not forcing but inching our seniors into a form of criminality. It concerns me greatly. And I think that's what would happen if given your choice, Mr. Chairman.

Chairman JACOBS. Well, that calls to mind W.C. Fields' comment that you can't cheat an honest man.

But if we live up to our highest ideals, and just the point, Bill, that you make that we feel better. Indeed, it improves our mental health. There is gratification in earning your daily bread.

I don't, just offhand, see why a good mentally healthy person, or a person who is not mentally healthy who wants to become mentally healthy, wouldn't choose to earn the $12,000 rather than receive it from Social Security, if that were the choice. I don't even mention work fare, but in another category in our society, it's considered generally admirable if a person receives welfare and gets out and rakes up some leaves or something for the community in return for it.

Now, on the question of the earned right. The earned right, as I understand it, since the inception of Social Security, was the right to collect retirement benefits if you happened to be retired. It never was, as I understand it, conceived as an annuity which happened with the passage of a certain number of years. Am I right about that—in the concept of the law, what the condition was while these people and you and I pay into the Social Security System.

Mr. **Archer**. Well, you're accurate about the initial implementation of Social Security in a sense that it provided for a loss of benefits if you continued to work. But you've got to also remember that the average life expectancy at that time was 61 years of age.

So there really wasn't much of a question of people continuing to work because most Americans died before they could draw their first benefit at age 65.

In addition, there was no early retirement at age 62. You had to reach 65 to draw a benefit. And the number of years that you were expected to live then was very short compared to what it is today. So I don't really think you can compare the two situations.

Another aspect, Mr. Chairman, is that you are treating Social Security really differently than you are other retirement programs in this country. You can say in the abstract if you had the choice between making $10,000 working or taking $10,000 in Social Security benefits, what would you choose? Different people would choose different things.

But when you are drawing, say, $12,000 in other types of retirement benefits, whether it be union pension plans, or company pension plans, or Federal military retirement or Federal civilian retirement, or many State retirement plans you don't place that same test on them.

Chairman **Jacobs**. But look at the consequence. What is the cost of civil service retirement based on? Would you care to say for the record?

Mr. **Archer**. Well, the cost is enormous.

Chairman **Jacobs**. Yes. It's 15 percent for Social Security, and it's inching up. I'd guess it's around 40 percent of the payroll for the Federal Government, but the man is rich because he has bayonets and can borrow.

Mr. **Archer**. But the point is that the worker is not paying that 40 percent. The worker is paying, as you and I know because we're covered under the civilian side, 7 or 8 percent of payroll, which is comparable to what the worker is paying under Social Security.

Chairman **Jacobs**. I appreciate it, but that gets back to earned rights. And you can't really say that what is paid for out of general revenue in the case of civil service retirement was an earned right. It is a conferred benefit on civil service retirees.

So, to compare Social Security with the civil service retirement, you would almost have to talk about a 20-percent Social Security tax for each worker matched by a 20-percent tax on each employer in order to meet that same level of benefits as an economic truism, it seems to me.

Mr. **Archer**. But the point is that the Federal worker is receiving, as you pointed out, considerably more in retirement benefits compared to what he or she paid in while working than a Social Security recipient is receiving.

Chairman **Jacobs**. Thank you. Mr. Schulze may have some more questions.

Mr. **Schulze**. Thank you, Mr. Chairman.

I do not have any questions for the gentleman from Texas, merely an observation. It seems a short 12 years ago when I served on the Social Security Subcommittee, and the gentleman from Texas at that time was a vocal proponent of the utilization of this dynamic asset of our Nation, our senior citizens, and was trying to work ways to keep them in the work force, and his ardor has not diminished over that time. He has been a champion of the issue and continues to be. And I appreciate his efforts.

Thank you.

Chairman JACOBS. Mr. Brown.

Mr. BROWN. Mr. Chairman, let me thank you for holding these hearings. My impressions have been that you are not the most enamored of any Member of Congress with the effort to eliminate this penalty and yet your fairness has prompted you to be willing to listen to the other side, and we very much appreciate it.

[Mr. Brown's opening statement follows:]

STATEMENT OF CONGRESSMAN HANK BROWN

Mr. Chairman, thank you for scheduling this hearing on the Social Security earnings test. My bill, H.R. 445 would repeal this earnings penalty by 1991 on Social Security recipients age 65 or older who wish to be productive.

The penalty is unfair to those who have contributed to Social Security and damages our economy. Rather than penalizing people for working, we should reward those who wish to work.

The law now requires that Social Security benefits be reduced $1 for every $2 earned in excess of an annual exempt amount. The annual amount now is $8,880 for persons age 65 to 70 and $6,480 for persons under age 65.

For example, if you are age 67 and earn $9,220 this year, you will earn $340 more than the exempt amount, and your Social Security benefits will be reduced by one-half of the excess or $170. The penalty is not applied to persons age 70 or older.

The earnings penalty is poor policy. First, it is difficult for some to maintain their pre-retirement lifestyles without working. They are caught in a cruel trap because by working, they will lose part of their benefits if they earn more than the annual exempt amount.

Second, our population is getting older. And as the population ages, the relative size of the work force grows smaller. With a relatively smaller work force, it will be more difficult for the U.S. economy to support those drawing retirement benefits.

Today, approximately 11.7 percent of the U.S. population is age 65 and older. In the next century, over 20 percent, or one-fifth, of the population will be of retirement age, according to actuarial figures in the Annual Report of the Board of Trustees of the Social Security Trust Funds.

Removing the earnings penalty for those over age 65 would allow those able to and interested in working to continue to do so without the fear of losing Social Security benefits. They could strive to maintain their pre-retirement lifestyles, without the current catch-22 to hold them back.

Leaving open the option to work will not only benefit our senior citizens, but the entire nation as well. H.R. 445 will open up an additional source of labor, as our work force grows smaller in relation to the overall size of our population.

This new labor supply will strengthen our economy, by providing needed workers. It also will ease some of the burden on the younger workers whose current contributions to the Social Security program help pay for the Social Security benefits received by our senior citizens. Those senior citizens who work will continue to pay FICA taxes on their wages, the same way they do today.

Just as important as the economic benefits is the effect this proposal will have on the morale of our senior citizens. Many people derive a good deal of satisfaction from their jobs. H.R. 445 will help them retain this feeling of being productive. It also will show them the nation still needs and cares about them, boosting their sense of self-worth. As a result, they are likely to be much happier and healthier individuals, with the positive by-product of lower medical costs for this population group as a whole.

With the elimination of the earnings test, CBO estimates the Social Security program would pay out from $4 billion to $5 billion in additional benefits each year. My feeling is that CBO's estimates are not accurate. Increased payments will be offset by both the FICA and income taxes paid on the wages of those senior citizens who work.

According to the Social Security Trustee's report, the Social Security Trust Funds are in good shape and expected to remain that way into the next century. H.R. 445 should improve those projections by increasing the ratio of workers to beneficiaries.

Those who complain this proposal will add to the federal budget deficit overlook the major pickup in taxes generated by the new earnings. The truth is that an increase in productive work will improve our economy, increase our competitiveness and stimulate federal revenue.

Those who want to work benefit us nationally and internationally. We are operating at close to a full labor market, and our supply of young workers has started to shrink. The retirement earnings test is a self-defeating public policy.

Historically, Americans always have been industrious. This attitude has made us a strong nation. We should be proud of this heritage and seek to preserve it. Repealing the earnings penalty does just that by encouraging our senior citizens who are both able and desire to contribute to society.

Mr. BROWN. Mr. Archer, what do you expect the consequences would be if this penalty were eliminated? What would happen? Would you see more work, less work?

Mr. ARCHER. Well, certainly we have every reason to expect, based on some of the projections that we see, that there would be significantly more people, particularly in the lower income categories, who would continue to work, who would be productive, some part time, some full time.

My mother-in-law is working part time in California, as is my father-in-law. They would like to work more. They are in good physical and mental health, but they reach that point and then they stop because they are faced with this scenario of paying the higher effective marginal tax rate of anywhere from 80 to 110 percent. And that's not just the result of the earnings limitation, but also that, in combination, as I mentioned earlier, with the payroll tax, the catastrophic illness income surtax, and the income taxation of 50 percent of Social Security benefits.

So this is one of the elements that really can't be considered by itself, that has to be taken in conjunction with the others. But, it's one that we have the capability to do something about. I think the estimates are that we would see perhaps upwards of 1 million Americans work who are currently working in some way or another, and that would certainly be of great advantage to them and to our society overall.

Mr. BROWN. I notice that there are some estimates that this would result in a loss of revenue. Not included in there is a calculation of the additional taxes that would come in, both State and Federal.

Not included in there, as I understand it, is the calculation of the additional Social Security taxes that would be paid. Not included in there is the adjustment that would come about by people who now choose to delay receiving their Social Security payments and thus generate a higher basis because of the delayed retirement provisions.

Do you have any estimate of what the real cost of eliminating this penalty would be?

Mr. ARCHER. Mr. Brown, we have never been able to get that information. We've asked for it over and over again. The Social Security Administration says that they do not have the capability to give us that. And the estimators in the other areas of the Federal Government have at least said they are unable to do it. And, as a result, we don't have those figures.

But certainly it's clear that the loss would occur for those who currently are working and forfeiting their benefits. That's where your revenue loss comes because then you would start paying them benefits.

But, on the other hand, for those who are receiving benefits today and not working, every single one of those who goes to work would not be a loss to the Social Security System but would, on the other hand, be a major gain to the system by virtue of the extra payroll taxes and a major gain to our economy overall generating significant additional new income tax revenues and sales tax revenues, excise tax revenues, revenues of all sorts, that would significantly impact on the budget deficit.

But we get no benefit in our proposal from any of those consequences.

Mr. **Brown**. Thank you. One last question and I will be brief.

One of the things that obviously we are going to be asked to do for those of us advocating this change is come up with the money. And the absence of a revenue estimate, of course, is devastating to us because it gives us a much heavier burden.

Do you see any tradeoffs that we can use in persuading those on the committee that may not be enamored with this proposal? Do you see any tradeoffs we can use?

Mr. **Archer**. Well, I have some tradeoffs that are in my legislation which I support. The immediate implementation of the 8-percent delayed retirement credit would generate significant additional revenue.

The provision that was in Senator Armstrong's bill that I discussed with the chairman earlier would generate additional revenue.

In light of the fact that we cannot get the benefit of the extra revenue that would be generated by people working, I do not have specific recommendations that would cover the entire cost of an immediate repeal. I believe it would cover itself if we got the true estimates. It's like what we dealt with in the capital gains arena over the years.

Those of us who believe in reducing the rate of capital gains have felt that it would generate additional revenue, that there was an optimum rate that was far below the 33 percent rate that is currently in the code.

Hopefully, some time in the near future we will get some of these feedback revenue estimates—that are justifiable—to effect this proposal. But certainly there would be enough revenue generated from those things that I have included in my bill, plus what Senator Armstrong has recommended, to significantly hike the dollar amount. If we do not get complete repeal, at least we ought to raise the threshold to as high a level as possible so that people can enjoy the fruits of their labors to a level beyond $8,880.

Mr. **Brown**. Thank you.

Mr. **Archer**. And maybe the chairman might look at that if you talk to him softly and firmly.

Chairman **Jacobs**. He cannot do that. He is running for the Senate. He has to start practicing.

I might say for the record that I am told that while CBO has not calculated the ratio between additional Social Security payroll taxes paid and benefits paid out, the actuaries of the Social Security System have, and they estimate that the loss would be on the order of 90 percent. The amount of payroll paid in would be 10 percent of the benefits paid, the additional liberalized benefits paid out.

I might also say for the record, Bill, you mentioned age 61, the life expectancy at the time in 1937 when the Social Security Act was passed. I am told that the number 65, the magic number of 65, began with Bismarck in Germany.

Mr. **Archer**. Bismarck. That is correct.

Chairman **Jacobs**. And they had a good thing going because, especially with all the wars they had, nobody lived to 65. But he was a pretty good politician. He got credit for one big goose egg.

Thank you very much.

Mr. **Archer**. Thank you, Mr. Chairman.

Chairman **Jacobs**. I think we should say for the record, too, I notice that the paper, I think this morning, has a glowing tribute of our colleague Bill Natcher. He is one of the really admirable Members of the Congress, and the man who just testified belongs right up there along with Bill Natcher, and I think Charles Bennett, too. We have three people who come to mind immediately who deserve the admiration of their countrymen, even Democrats.

Mr. **Archer**. Thank you, Mr. Chairman. The feeling is mutual. I would put you up there, too. Thank you very much.

Chairman **Jacobs**. Mr. Armey is next. I will say some nice things about you, too, Dick. With you, it is not a Democrat and a Republican. It is an Army and Marine Corps. Proceed.

STATEMENT OF HON. RICHARD K. ARMEY, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF TEXAS

Mr. **Armey**. Thank you, Mr. Chairman, and let me thank you for holding these hearings. I want to thank the other members for being here and express my gratitude for giving me what I consider to be the privilege of following the ranking Republican from Texas, Mr. Archer, who is sort of a personal hero of mine, especially on this issue.

Mr. Chairman, let me just tell you a little bit about my perception on this. It is very confusing for any of us to determine what is Social Security, what is it intended to be, what has it been intended to be in the past. Is it an annuity or is it a supplement or whatever? I feel compelled to represent what I perceive to be the perception of Social Security by the senior citizens in my district.

Let me say that the senior citizens in my district count very few, as it were, elderly bag ladies and very few wealthy retired citizens. For the most part, my retired citizens are skilled, blue-collar working men and women. They are people who have a perception of Social Security which is not necessarily very appreciative of nor complimentary to the system.

I would say from the experience I have in my district in dealing with my seniors in our senior centers and around is that if there is any group of Americans that have an anger toward the Social Security System, which they are not the least bit reluctant to express, it is the seniors themselves. They perceive Social Security as a mandatory retirement program to which they were compelled by the Government to subscribe in lieu of what they believe would have been better alternatives in the private sector. As such, they believe very strongly that they ought to be able to exercise the same discretion and control over their retirement destiny, or semiretirement destiny, that they would be afforded and be compelled to be afforded by the Government in the private sector. And they have an enormous resentment over being treated as wards of the State.

They have pushed me forward on this issue. Certainly, I have many great and influential and thoughtful colleagues to follow while I am here in this town. But as I then look at their testimony and their experience, I like to reflect back on what I consider to have been one of the greatest privileges I have had since I have been in this body to be asked, called in my office and asked by Claude Pepper himself if I would be willing to go to the floor and speak on behalf of his legislation banning age discrimination. I thought that was a great honor, and obviously Claude Pepper is a man for whom we have a great deal of affection and respect and a man who has managed to keep his wits about him and be quite effective as a legislator well into his eighties. He is himself a living demonstration of the productivity we can have from our senior citizens.

So the first thing I see when I look at the Social Security earnings limitation is a remaining vestige of age discrimination. And that, I think, is very compelling to me.

The senior citizen, frankly, just simply should not be compelled to suffer as much as a 50-percent specific tax levy for wanting to continue to work. At the same time, I see a loss of valuable workers that can influence the whole economy.

You know, I thank you, Mr. Chairman, from what I know of you and your personal values, the spirit of workmanship is probably the foundation to a labor force with productivity, people who understand their duty on the job and are willing and cheerfully able to do that, carry that out. Seniors, I think more than any other instructional source available to us, are capable of teaching these lessons of the spirit of workmanship to younger workers.

As a matter of fact, especially with respect to the kind of seniors that I represent, I think in particular of a group of retired craftsmen. These are blue-collar machinists that have retired but still retain their energy and their vigor and their willingness to work.

At the same time, the Nation is screaming for machinists. You have here an occupation that has been traditionally an occupation where apprenticeship arrangements have been the manner in which the skills were taught, and yet we have this specific group of skilled workers who are eager to continue to work and who could best teach young workers not only the spirit of workmanship but the skills on the job that are being, I think, encouraged, if not compelled, to stay out of the work force.

I know that there are many proposals that are offered by various Members of Congress. Mr. Wyden and I are working on a proposal, and we are trying to be aware, as we develop our proposal, of what your most compelling difficulty is: How do you pay for any change in this legislation?

We believe that it is probably not possible, from a fiscal point of view, to have an outright repeal of an earnings limitation, and that I think there are probably some egalitarian reasons why one might be averse to doing so. But certainly I think we should be able to find it within the law, within the budget, and within our hearts to raise this cap.

If I might just take a moment to relate to the question you asked Mr. Archer earlier about the choice given to earn $12,000 or to have $12,000 as part of your earned annuity, which most of my citizens believe it is, their right that they paid for—and they are very clear on that.

Chairman JACOBS. Did they ever read the law?

Mr. ARMEY. They are very clear on that, and they do not really feel as though we are. But my seniors, like most people, work to eat.

Quite frankly, I have to tell you, Mr. Chairman, there are very few people that I have encountered in my lifetime that work out of preference. We work because we have to. And most seniors who come to me and talk about the desire to continue working in their golden years are saying, "I cannot survive. I must have more money for myself and my wife and for the things that we hoped and dreamed we would be able to have some time to pay the taxes so we do not lose our house."

So I would suggest that my seniors are saying, "Please give me an opportunity, if I am making this minimal income on my retirement program, to continue working while I have the energy and I have the skills, and let me take my income without extra prejudice under the tax laws."

I think that as you go forward and examine the manners in which we might be able to get offsets and revenue increases through an increase in the limit, that would allow these middle-income skilled workers continue to work without prejudice, that you should, I would hope, be able to work out the numbers.

I appreciate the fact that that is your job and not mine. It will be a difficult job. But I am very confident that when you weigh what will turn to be in a more dynamic model a far less deterrent revenue loss than what we suppose at first blush, against the fundamental principle of giving support by our Government to our own Government's legislation which bans age discrimination, that the egalitarian impact of that on a principle which I happen to believe deserves our total support will more than compensate the public interest for the revenue loss that you may experience when it all nets out.

Let me just say, finally, Mr. Chairman, I guess my earliest experience with that, this whole question, was when between the ages of 65 and 72, my early adolescence and into my most early adulthood, I learned about tools, about working, about enjoying the use of my hands for creative purposes from a kindly old gentleman who worked in the garage behind our house and who never thought that it was the Government's business to interfere with his doing, in those years, all he had done all his life. I do not know what fiscal arrangements he made between himself and the Government, but I knew him to be a honorable man who taught me a great deal that I am now able to teach my children. And I should think this is a resource we ought not to let be lost to our children and our grandchildren.

Thank you for letting me testify.

[The statement of Mr. Armey follows:]

The Honorable Dick Armey
Subcommittee on Social Security
May 25, 1989

Mr. Chairman and members of the subcommittee, thank you for allowing me to testify before you today as part of this important hearing on the Social Security Earnings Test.

I wholeheartedly support the growing movement which is seeking to reform and/or eliminate the Social Security Earnings Test in order to take away the disincentives now built into our Social Security system. Older Americans who must work to make ends meet, or simply wish to work, should be able to do so without paying exorbitant taxes on earned income that they use to supplement their monthly Social Security checks.

There are no less than one dozen bills pending in the House which propose to do just that. Some of the bills call for the immediate repeal of the Earnings Test, others call for the gradual elimination of the Test, and there are a few which seek to raise the amount of exempted income to take the burden off the backs of the working elderly. The sheer number of bills and the diversity of their cosponsors is ample testimony to anyone who doubts that this is an idea whose time has come.

Workers between the ages of 62 to 69 are subject to this onerous tax which causes individuals with more than 8,880.00 in earned income to lose one dollar in benefits for every two dollars earned. This effectively imposes a 50 percent tax rate on income above the exempt amount. This high marginal tax rate, which does not apply to any other class of Americans, is patently unfair and creates an unfair burden on the sector of our population which can least afford it, the elderly worker. We must take action to alleviate this problem, and begin taxing elderly workers at the same rate as their younger counterparts in the workforce.

After all, the real irony of this Earnings Test is that the high marginal tax rates do not apply to wealthy older Americans who can make millions per year in unearned income without being subjected to higher tax rates which are only directed at the middle and lower income groups. In fact, the National Center for Policy Analysis, of Dallas, Texas, in a recent report calculates that the Earnings Test is a key factor in creating the highest marginal tax on the middle class in our country's history. The report further indicates that due to the high tax rates on wage income for elderly workers, many older Americans will be unable to earn enough additional money to pay the new catastrophic health care surtax and maintain their 1988 standard of living in 1989. This is a sad state of affairs.

As a representative body, we cannot overlook the implications of our current discriminatory policies. The Earnings Test, quite simply is age discrimination. At a time when American competitiveness is at the forefront of national debate, our most underutilized resource is the productive capacity of the millions of older citizens. The knowledge and experience of these potential workers is going completely to waste. Let's join together and repeal the Earnings Test and give these people the opportunity to make a choice for themselves. We need to lower the marginal tax rates and provide an incentive for the elderly workers to re-engage their productive capacities on their own behalf and that of the country as a whole. Take away the penalty for working and re-start the engines of progress.

One major question which must be addressed as part of any plan to alter the current system is funding. How will we pay for it? Where will the money come from? I would like to suggest that depending on which avenue we decide to pursue, the repeal of the Social Security Earnings Test may pay for itself. To begin with, we will save approximately $200 million dollars in administrative costs. Further, we can expect a large movement back into the labor force by elderly workers who have been strong-armed to the sidelines by this unusually effective deterrent to continued employment. Although, as an economist, I am painfully aware that we cannot predict the future with any degree of certainty, I nonetheless believe that several hundred thousand individuals would find their way back into the work force if we abolished the Earnings Test. The resulting increased productivity followed by increased tax revenues would go a long way toward funding this legislation.

This is a perfect example of the skewed predictions we get when we depend on static analyses instead of dynamic models. Static analysis does not take into account the "human factors." When individuals are given incentives to produce, by the elimination of economic barriers such as prohibitively high tax rates, a dynamic analysis will better predict potential results in the area of increased productivity and increased tax revenues.

But leaving aside the budgetary considerations for a moment, I would suggest that we approach this legislation from another perspective. What is right and proper? That answer is clear to anyone who has looked closely at this intolerable situation. The withdrawal of the elderly from the labor force is accelerating. Among those 65 years old, the retirement rate has increase by 40 percent between 1970 and 1985. The Earnings Test must go and now is the time to remedy this flaw in the Social Security system. There is no justification which can withstand scrutiny for taxing elderly workers at a higher marginal tax rate based only on their dates of birth. Let's allow our older Americans to again participate fully in the nations economy.

Thank you again for allowing me to testify before the subcommittee today.

Chairman **Jacobs**. Thank you, Mr. Armey.

Mr. Schulze.

Mr. **Schulze**. Again, Mr. Chairman, in the interest of time, I have no questions other than to thank our colleague for very cogent testimony. I know it is an issue he believes in very deeply and strongly because we have discussed it in other forums.

Thank you.

Chairman **Jacobs**. Mr. Brown.

Mr. **Brown**. Thank you, Mr. Chairman. No questions.

Chairman **Jacobs**. Dick, you expressed a concern about wretchedness in old age and inadequacy of income. Were you here when Mr. Archer and I discussed the older elderly, the octogenarians who in many cases with SSI receive as little as $4,000 a year?

Mr. **Armey**. Yes.

Chairman **Jacobs**. The retirement test next year is scheduled to be about $10,000. The family that has, say, $10,000 in Social Security benefits paid annually therefore would have about a $20,000 a year income. If the Armstrong proposal passed, I assume that would mean that some families would have a $21,000 rather than a $20,000 income.

My question is: Do you think the $1,000 is better spent on the $20,000 income than it would be on the $4,000 income for the octogenarian retired?

Mr. **Armey**. Well, you know, of course, as an economist, you have posed the classical question of public policy, which is the fact that there must be a tradeoff. The question is: Is the gain to the gainer greater than the loss to the loser? And I think if, in fact——

Chairman **Jacobs**. No, I think you misperceive my question. The $4,000 person would not lose anything.

Mr. **Armey**. She would not lose. She would not have gotten.

Chairman **Jacobs**. Right.

Mr. **Armey**. If I were sitting in your seat and I were forced with that tradeoff with no way to bring in a third variable, I think I would be compelled to act on behalf of that group of citizens that might be forced to——

Chairman **Jacobs**. I just have one other question. Take the person who, let us say, earns $30,000 per year. He or she is 60 years old, cannot have any benefits from the Government, certainly not Social Security. What is it about the arrival of the age of 62 or 65 when that person still could not have benefits that would make that person give up the $30,000 a year if the person wanted to continue working?

Mr. **Armey**. Well, this is something I try to study a great deal. I cannot perceive of myself ever retiring at any age. If I am lucky, I will die in my traces; you know, they can cut me out and pull me over to the side and go on.

I think it becomes a matter of energy with a lot of seniors. They have to start trading off the amount of energy they have for the recreation and the enjoyment that they had always hoped to have in those years to continue to work on the job. And I think most seniors would like to move to some kind of a middle ground where they can continue using their skills, continue being involved in the world of work, but more on a part-time basis.

Chairman **Jacobs**. Well, by coincidence, the $10,000 of income permitted while a person is still deemed retired, and the person receiving $10,000 in Social Security sounds pretty middle-groundish to me?

Mr. **Armey**. I understand. But, again, I think you have to go back to the point, and I see it with my mother-in-law and father-in-law, and I see it with a lot of my seniors in the senior centers. They simply do not feel that they can live on what they are legally able, but I also think there is another point that I see expressed. It is an anger.

You know, I have become convinced in my mind that if there ever develops a militant constituency in the near term for the privatization of retirement, which we used to on occasion call the phasing out of Social Security—and the most foolish of us might have even said abolish Social Security, which would be devastating.

But if there becomes a militant constituency for that, and if there is one developing, I see it in my district among my seniors. I made reference to it earlier.

We have here people that have responsibly supported themselves and their family throughout a lifetime who feel all of a sudden as if they are being treated as if they were wards of the State, and even though my offices in my district—and I am sure in your district—the staff are sensitive and caring people, the redtape that they must endure, the Social Security Administration, is an aggravation.

So they are saying, "Let me have my choice free and away. If I go out and earn a dollar, let me keep it with no more tax impact than what I would have suffered had I been 55 and earned that dollar."

Chairman **Jacobs**. Why is the lack of the Government benefit which you did not pay for under the terms of the contract when you paid the Social Security tax—you are not getting the benefit that you never paid for—how is that lifted across the bar to become a tax? I have heard that a lot lately, but I am not smart enough to quite grasp how the failure of Uncle Sam to give you something suddenly is a tax. Why is that?

Mr. **Armey**. Mr. Chairman, I posed that question rhetorically in one of my senior citizen centers one time. They did not make me smart enough to know the answer, but they made me smart enough not to pose the question again.

Chairman **Jacobs**. Well, I will pose the question. I think I am just barely smart enough to pose the question.

I think for 30 years I have paid substantial premiums to the Allstate Insurance Co. on my automobile, and so far I have not collected a penny because the condition of the contract is that something has to happen before I can collect anything from the premiums that I have paid in. That is known as an accident, some damage done, in which case they become legally obligated to compensate me.

Now, it is always a gamble, and I hope I continue to lose. Should I be angered and militant because of paying literally thousands and thousands of dollars now to my insurance company, and I do not get anything back? Is there a difference when there is a condition to Social Security for retirement benefits and a condition to automobile insurance for benefits paid? What is the difference?

Mr. BROWN. Mr. Chairman, would you yield on that?

Chairman JACOBS. Yes. If Mr. Armey will yield.

Mr. ARMEY. Well, surely.

Mr. BROWN. Just a quick observation. I would be happy to loan you my teenage son, who I believe could take care of your problem with your insurance company very quickly. [Laughter.]

Mr. ARMEY. As a matter of fact, I have a few I could throw in for you. You would catch up in a big hurry.

Mr. BROWN. The chairman is working on this problem himself, and I think that is the best way to handle it, I guess. But I think it is only natural and understandable people would look at the comparative results. If they work, where are they? If they do not work, where are they? That is part of what is most disconcerting about this particular aspect of Social Security as we have built in a penalty for people working and producing and being creative and productive.

Chairman JACOBS. But why is the failure of the Government to give you a benefit that you never paid for a penalty? You can carry that logic across the spectrum.

Mr. BROWN. Precisely because if you do not work, you are entitled to the payment. It is only when you do work and help out your society and your country and become productive that you lose it under the terms of the policy.

Chairman JACOBS. But was that the condition under which you paid your Social Security taxes? Was that not in the law along when you paid?

Mr. BROWN. But you surely would not deny us an opportunity to improve the country.

Chairman JACOBS. I do not know. We have been improving the country about 200 billion dollars' worth of deficit a year this decade. I do not know whether we can stand much more improvement.

Mr. Armey is entitled to answer the question.

Mr. ARMEY. I appreciate the point. Mr. Chairman, I have to tell you—and, again, I think this becomes a problem in terms of—you seem to be very clear in your understanding of what Social Security was conceived to be, what it has been, and what it is today. That is a clarify of understanding I do not often find. I am not surprised that you would be very clear in your own——

Chairman JACOBS. Surely they can read in Texas as well as in Indiana. The law is quite clear. You have to be retired to collect retirement benefits, and the retirement test by which you are deemed retired is going to be $10,000 next year. You can earn $10,000 and still say you are retired next year.

Mr. ARMEY. Mr. Chairman, I guess I would have to, in deference to the literacy of Texas, point out that Texas has just had a couple of pretty painful lessons in the old adage perception is reality. I guess my Texas seniors would say, "We perceive Social Security to be a bought and paid for right that should be"——

Chairman JACOBS. Which is clearly defined in the law, the right.

Mr. ARMEY. By right. And I paid in those annuities, and now you may say the seniors are engaging in a behavioral pattern that was not anticipated by the Government. But I more often than not will find seniors who will tell me, "I never intended to be made to be retired and stay out of the work force or suffer prejudice under the Tax Code. And if that is what you and the Government intended"—I always get a kick out of it when I have a 65-year-old man tell me about laws made in his adulthood, in my childhood, and hold me accountable for it. They are pretty tough folks. I am amazed that you can talk in terms of a right to a payment or a receipt that they did not pay for, because their perception is very clear.

I feel duty-bound to represent the perceptions of my constituents, and they are very militant in this perception.

Chairman JACOBS. Right. Just one final question, Dick. Are there any other entitlement programs you would like to liberalize?

Mr. ARMEY. I would like to liberalize what we call generally welfare. I think there are many, many ways with true compassion and understanding this Nation could, in fact, take care of our truly needy—that is, low-income Americans. I differentiate between the needy and the greedy—and save the taxpayers money while giving, for example, the young welfare mother a real opportunity to do better in supporting her children and herself.

There are a lot of programs that I think need serious reform.

Chairman JACOBS. We thank you for your testimony. We had two Texans in a row, so I guess I will have to say for the record that the old story is that you never ask a person if he is from Texas. If he is, he will say so. And if he is not, do not embarrass him. Is that right?

Mr. ARMEY. I do need to go back to your last question and point out that I would respond to the question better had it been said are there any welfare programs in addition to Social Security, which is not a welfare program.

Chairman JACOBS. I understood that. Thank you very much for your testimony.

Helen is next. Where did she go?

[No response.]

Chairman JACOBS. We will take Mr. Coble next. Then if Helen comes back, she can go then.

STATEMENT OF HON. HOWARD COBLE, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF NORTH CAROLINA

Mr. COBLE. Mr. Chairman, thank you. I appreciate your conducting this hearing, Mr. Chairman. It is good to be here. I will not bore you all by reading my statement. With your permission, I would like to paraphrase it.

As you all know better than anybody in this room, this issue has been before the Congress for about two decades. I am one of several Members who has introduced legislation to address this earnings problem, hopefully remove it. My bill would raise the earnings limit by $3,000 per year, phasing it out altogether after 1995.

In a nutshell, Mr. Chairman and Mr. Brown, here is why I think that repeal, or at least revision, is warranted:

First, the test is confiscatory. Combining its effective marginal surcharge with other Federal taxes, a person could forfeit 80 cents out of every dollar earned to the Federal Government.

Second, the test creates a mandatory retirement bias. Many older Americans want to continue working but have the fear of losing benefits to which they are otherwise entitled if they do.

Third, the test denies the economy the benefit of millions of experienced workers, particularly at a time when the composition of the labor force is changing. This has been touched on before. I think Americans over 65 provide a seasoned, skilled, experienced element of the total work force.

And, fourth, the test is a major manpower burden on the Social Security Administration. I am advised that it requires the equivalent of 2,500 employees working full time each year to handle matters relating to the earnings test. Most of the overpayments and a great many of the underpayments of benefits are due to earnings test miscalculations. This confusion, combined with the high marginal tax rates, have compelled many older Americans to join the ranks of the underground economy.

I know there has been much concern about the cost of effecting a repeal or substantial revision. But most of the estimates I have heard or seen do not include the offsets of additional income tax and FICA revenue. Nor do they adequately take into account the number of underground workers who might begin reporting their additional income.

Finally, in conclusion, it is easy for us to get lost in a maze of numbers and abstract ideas on Capitol Hill. To acquire a genuine sense of how legislation affects real people—those beyond the Beltway—I find it beneficial to solicit their opinions.

Mr. Chairman, I would like to read a letter that I recently received from one of my constituents, Mrs. Shirley Booth of Greensboro, NC, and I have her permission to read this to you. She wrote to me:

> No one can live on (Social Security) alone, and with four children to raise by myself, I was not able to put much aside for retirement. Now I have to work part-time in order to continue making house payments plus all the regular bills. * * * With some employers begging for elderly people to work because they are more dependable (we were brought up that way—to work hard).

She writes:

> It does not make sense for the law to limit the amount of money you can make. * * * Many would love to work; many need to work for financial and emotional reasons. So why not let us work while we are still able * * *?

Mr. Chairman, I appreciate your conducting this hearing and for permitting me to appear before you.

[The statement of Mr. Coble follows:]

STATEMENT BY THE HONORABLE HOWARD COBLE
BEFORE THE HOUSE SUBCOMMITTEE ON SOCIAL SECURITY
REGARDING THE SOCIAL SECURITY EARNINGS TEST

MAY 25, 1989

Mr. Chairman, I promise to be brief. First, I want to thank you for holding this hearing on the possibility of liberalizing or repealing the Social Security earnings test. This issue, as you are aware, has been debated in the Congress for nearly 20 years; but at no time, in my opinion, has there been a more unified effort, as there is now, to revise existing law in a major way.

I am one of several members who has introduced legislation to do just this. Last term I sponsored Senator Armstrong's bill on the House side, and reintroduced this same measure earlier in the year. The bill, H.R. 841, would raise the earnings limit by $3,000 a year, phasing it out altogether after 1995. It would also accelerate the 8% delayed retirement credit to 1995. Naturally, I hope that it generates some interest with you and your colleagues. If not, I further hope that you will devote your attention to Representative Hastert's bill, which is cosponsored by more than 100 members, including myself.

In a nutshell, I think repeal is warranted for four reasons:

- First, the test is highly confiscatory. Combining its effective marginal surcharge with other federal taxes, a person could easily forfeit eighty cents to Uncle Same on every dollar earned.

- Second, the test creates a mandatory retirement bias. Many older Americans want to continue working but are afraid of losing benefits to which they are otherwise entitled. The government should not force older Americans to rely on Social Security as their sole source of retirement income.

- Third, the test denies the economy the benefit of millions of experienced workers, particularly at a time when the composition of the labor force is changing. The baby boom is over, and many employers are making a conscious effort to recruit older Americans for jobs that at one time were filled by much younger workers. Experienced, reliable workers -- older workers -- will always be in demand.

- And fourth, the test is a major manpower burden on the Social Security Administration. It requires the equivalent of 2,500 employees working full-time each year to handle matters relating to the earnings test. Most of the overpayments, and a great many of the underpayments, of benefits are due to earnings test miscalculations. This confusion, combined with the high marginal tax rates, have compelled many older Americans to join the ranks of the underground economy.

I know there has been some concern raised about the cost of effecting a repeal or substantial revision. But most of the estimates I have heard or seen do not include the offsets of additional income tax and FICA revenue. Nor do they adequately take into account the number of underground workers who might begin reporting their extra income. I would certainly welcome any light the subcommittee can shed on this matter. In addition, I think we must all acknowledge that cost, while important, is not the only consideration that should be taken into account before arriving at a decision.

Finally, it is easy to get lost in a maze of numbers and abstract ideas on Capitol Hill. To acquire a genuine sense of how legislation affects real people, I find it beneficial to solicit their opinions. Here is what one of my constituents, Ms. Shirley Booth of Greensboro, North Carolina, has to say about the earnings test:

> No one can live on [Social Security] alone, and with four children to raise by myself, I was not able to put much aside for retirement. Now I have to work part-time in order to continue making house payments plus all the regular bills.... With some employers begging for elderly people to work because they are more dependable (we were brought up that way -- to work hard), it does not make sense for the law to limit the amount of money you can make.... Many would love to work; many need to work for financial and emotional reasons. So why not let us work while we are still able ...?

Mr. Chairman, I urge you and your colleagues to expedite consideration of a bill to repeal or revise the earnings test. Thank you again for allowing me to appear before you today.

Chairman JACOBS. Thank you, Howard.

Mr. Brown.

Mr. BROWN. I am wondering if you have a different feeling about those who have retired early, before 65, in regards to this penalty than you do for those who retire after 65.

Mr. COBLE. Well, Mr. Brown, I would put the ones who retired after 65 on the front burner, with most direct attention. They are the ones I would give preferential treatment to because the others have optionally exercised their right to retire early.

Mr. BROWN. Well, I must say I share that view, and it strikes me that maybe one of the ways we can pay for this is by looking at that kind of tradeoff.

I thank the gentleman for his excellent statement.

Mr. COBLE. Thank you, sir.

Chairman JACOBS. We thank you for your contribution. Have a nice weekend.

Mr. COBLE. Thank you, Mr. Chairman.

Chairman JACOBS. Mr. Rowland, John Rowland, our colleague who works out in the gymnasium every morning of his life. He is right about that.

STATEMENT OF HON. JOHN G. ROWLAND, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF CONNECTICUT

Mr. ROWLAND. Thank you very much, Mr. Chairman.

Many excellent points have already been covered, so with your permission, I will just summarize my statement.

I first thank you for the opportunity to testify this morning. It is, indeed, a critical issue, the mere fact that we have had so many Members willing to step forward and make remarks is evidence of its importance. This issue is going to affect millions of older Americans. And I think it is going to significantly impact our Nation's industrial productivity.

I think if you look at the history of the Social Security Act of 1937 and give it the strongest reading possible, it reveals the true intent of the earnings test. And I think we need to look at that. Older workers were to be given a strong incentive to retire at that time in order to provide employment for millions of younger Americans that were made jobless by the depression.

In 1937, that was sound policy. It was good social policy. But, indeed, times have changed significantly, as highlighted throughout the testimony today.

I would be very surprised, Mr. Chairman, to learn that any Member of Congress has not been deluged with statistics and reports and analyses of the impeding shortage of skilled labor which our Nation faces. How can we defend a policy that encourages our most skilled and experienced workers to leave the workplace? It makes no sense whatsoever.

The problem workers discover after they have retired is that their pensions and their other payments are often not enough to meet the daily cost of living. The most obvious example of this is the skyrocketing costs of health care. In order to cope with these costs, older Americans often seek to return to work typically in a part-time position, and many times full time. As Mr. Schulze highlighted, in most instances these workers want payment under the table or in some way to avoid the earnings test.

Then comes the Social Security retirement test. The Government says: Go ahead, reenter the work force, but don't think about earning enough to cover your costs. How many of us have successfully explained to our constituents that Uncle Sam needs $1 for every $2 they earn over certain income levels so that we can pay for future benefits and reduce the Federal deficit? The vast majority of these retirees end up dependent on Social Security, Medicare, and after spending all their assets, Medicaid benefits then kick in. Liberalizing the earnings test would certainly brighten the picture for these forced retirees.

For those who claim that liberalizing the earnings test would cost too much money, I say that they are being shortsighted. Whatever option is chosen, of course there will be startup costs. But I think we need to keep in mind, as mentioned this morning, that these are only short-term costs and that in the long term substantial revenues will be gained.

For example, workers who remain actively employed are workers who are contributing payroll, FICA and other taxes. Added to that are the horizontal benefits of more productive companies that also pay taxes, and the service industries that specifically benefit from income-earning workers and companies.

If the subcommittee is determined that offsetting revenues must be offered for any liberalization, I point out the billions of dollars that businesses lose annually due to worker absenteeism. Older workers have been proven in study after study to be more dependable and less likely to be purposely absent from work. It seems ironic to me that the Japanese worker, whose productivity and business dedication we marvel at these days, learned much of his skills by adopting and building upon American workplace models that were manned by the very workers that the earnings test will impact.

In closing, Mr. Chairman, U.S industrial competitiveness and productivity cannot afford the present Social Security retirement test. When the labor crisis becomes more widespread, Congress will be forced to do something about this onerous problem. I would only hope that armed with the testimony you have received today, the subcommittee will move to play a more progressive role. For those truly concerned about our twin trade and budget deficits, paying now is far better than paying later.

Thank you very much, Mr. Chairman and members of the subcommittee. I will be glad to answer any questions you might have.

[The statement of Mr. Rowland follows:]

STATEMENT OF CONGRESSMAN JOHN G. ROWLAND
before the
SUBCOMMITTEE ON SOCIAL SECURITY
of the
COMMITTEE ON WAYS AND MEANS
May 25, 1989

Chairman Jacobs and Members of the Subcommittee:

I would like to express my appreciation to the Subcommittee for permitting me to testify today regarding the Social Security retirement test, commonly referred to as the "earnings test." This is a critical issue that not only affects millions of older Americans, but also significantly impacts our nation's industrial productivity. It is my fervent hope that this hearing will hasten the liberalization of the earnings test. Chairman Jacobs, I commended for providing such an opportunity.

My distinguished colleagues who preceded me have aptly detailed the many reasons why the earnings test should be liberalized. However, I believe that certain points deserve reiteration and reinforcement.

Mr. Chairman, how can the United States ever expect to regain its status as the world's foremost economic power if by our own government's policies we prevent the most experienced and dedicated workers from being able to fully contribute to the economy? How can the U.S. expect to maintain the economic momentum it now has, if we continue to forcefully reduce the pool of skilled workers that is available?

Even the most cursory reading of the history of the Social Social Security Act of 1935 reveals the true intent of the earnings test. Older workers were to be given a strong incentive to retire, backed by social security benefits, in order to provide employment for millions of younger Americans made jobless by the Great Depression. In 1935 that was sound policy. By 1989, that policy has become an anachronistic disease afflicting American industry and this nation's economic well-being.

Instead of recognizing the dramatic demographic changes which have occurred over the last fifty-four years, successive Congresses and administrations have resorted to a sadly enduring policy, approving quick fixes and politically sufficient incremental adjustments in place of necessary reforms. The result is well known - the problem becomes institutionalized and efforts are directed toward making up excuses to maintain the status quo.

Today the excuse is the budget deficit. Regretfully, it is a handy excuse which Congress will milk bone-dry until enough of us stand strong and resist it. Every Member of the House has signaled his or her support for restoring U.S. industrial competitiveness. I am determined to test their support and liberalizing the Social Security earnings test is an appropriate place to begin.

I would be very surprised, Mr. Chairman, to learn of any Member of Congress who has not been deluged with statistics, reports and analyses of the impending shortage of skilled labor which our nation faces. As a Member from a New England state, let me qualify that statement by saying the labor shortage is already here and it is fast reaching crisis proportions. During a time when the politically "hot" topic to expound upon is how America needs to reenergize its industrial productivity and competitiveness, it is hard to defend a policy that encourages our most skilled and experienced workers to leave the workplace.

There are two related issues in today's workplace which, in conjunction with the earnings test, compound the larger competitiveness issue. They are the pre-retirement factors of age discrimination and the growing use of early retirement policies to facilitate corporate down-sizing or restructuring. The first problem is more readily mitigated by labor supply and demand changes, but the second is a disturbing trend that must be actively fought. While I accept that many workers actively seek early retirement, there are literally millions of older workers, with productive years still to contribute, who opt to retire because they cannot overcome these obstacles or afford any related consequences.

The problem workers discover after they have retired is that their pensions and other payments are often not enough to meet their daily cost of living. The most obvious example of this is the skyrocketing cost of health care. Health care inflation is running conservatively at twice the rate of the consumer price index and in most instances three, four or more times faster. In order to cope with these costs older Americans often seek to return to work, typically in part-time positions, but often full-time.

Then comes the Social Security retirement test. The government says, "go ahead reenter the workforce, but don't think about earning enough to cover your costs." How many of you have successfully explained to your constituents that Uncle Sam needs $1 for every $2 you earn over certain incomes levels so that he can pay for future benefits and reduce the federal budget deficit? Even in 1990, when the take is only $1 for every $3 earned, the task will be no easier. Remember, these are the constituents who write to tell you that they must often choose between going to the doctor and having three square meals-a-day.

The vast majority of these retirees end up dependent on social security, Medicare, and after spending their assets, Medicaid benefits for their daily existence. I challenge anyone to paint a bleaker picture of the retirement, or "golden" years for these proud, hardworking Americans -- the Americans who made up the backbone of this nation's industries. Liberalizing the earnings test would certainly brighten the picture for these forced retirees.

I should make clear here that the earnings test issue is not one of wealthy versus low-income retirees. Wealthy retirees typically have "unearned" income that is not even affected by the earnings test. The retirees at issue here are like those in my hometown of Waterbury, Connecticut and other towns in my district, who worked hard all their lives to buy a house, a car, raise children and send them to college, and save something for their retirement. Today, their retirement dreams are shattered and they must keep on working just to maintain themselves and their dignity. The social security earnings test hits these Americans the hardest.

For those who claim that liberalizing the earnings test would cost too much money, I say they are being shortsighted. Whatever option is chosen (repealing the earnings test at an earlier age or increasing the earnings test amount) there will be start up costs. We must keep in mind, however, that these are only short-term costs and that in the long-term, substantial revenues will be gained. For example, workers who remain actively employed are workers who are contributing payroll, FICA and other taxes. Added to that are the horizontal benefits of more productive companies that also pay taxes, and the service industries that also benefit from income earning workers and companies.

I will be the first to admit that figures on the level of revenues to be gained are not easily quantifiable. Many of the variables that make up an older worker's decision to retire are subjective and can change. Rather than undermine my argument, I believe that this point actually bolsters it. Is it not equally reasonable to expect that employed workers are more likely to have health and benefit plans, and would therefore represent a reduced burden on the social security, Medicare and Medicaid programs? Liberalizing the earnings test will ensure that there are more workers than retirees and thereby create surplus revenues.

If the Subcommittee is determined that offsetting revenues must be offered for any liberalization of the earnings test, I point out the billions of dollars that businesses lose annually due to worker absenteeism. Older workers have been proven in study after study to be more dependable and less likely to be purposely absent from work. It seems ironic to me that the Japanese worker, whose productivity and business dedication we marvel at these days, learned much of his skills by adopting and building upon American workplace models that were manned by the very workers the earnings test is now forcing into early retirement.

In closing, Mr. Chairman, U.S. industrial competitiveness and productivity cannot afford the present Social Security retirement test. When the labor crisis becomes more widespread, Congress will be forced to do something about this onerous problem. I would only hope that armed with the testimony you receive today, the Subcommittee will move to play a progressive and prophetic role in closing the chapter on the earnings test. As the salesman on television says, "you can pay me now, or you can pay me later." For those truly concerned about our twin trade and budget deficits, paying now is far better than paying later.

Again, thank you Chairman Jacobs and Members of the Subcommittee for allowing me to testify before you today.

Chairman Jacobs. Mr. Brown.

Mr. Brown. I just want to commend the gentleman on his statement and observation. I think particularly his insights on the reasons that the earnings penalty was passed originally are very revealing and particularly appropriate to current days, where I believe the penalty reduces worker productivity rather than the contrary.

Chairman Jacobs. I am happy that you took the trouble to make the appearance, too, John.

Mr. Rowland. Thank you very much.

Chairman Jacobs. Have a happy weekend.

Our next witness is our colleague Mr. Hastert of Illinois.

STATEMENT OF HON. J. DENNIS HASTERT, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF ILLINOIS

Mr. Hastert. Thank you, Mr. Chairman. I certainly appreciate the opportunity to testify before you today and for your taking your time to listen to the whole parade of us coming before you. I think you have heard a lot of arguments and are well aware of the issue.

Chairman Jacobs. I love a parade. [Laughter.]

Mr. Hastert. For that reason, I am going to forgo reading my testimony and just try to discuss some of the issues that I think are really important and cogent.

Yesterday, I introduced a bill in the House of Representatives with 120 original cosponsors on it, and it was a pretty generic bill. We did that for a reason. The bill said that anybody between the ages of 65 and 69 would be free of the earnings test. One of the reasons we did that—and we worked with the Social Security Administration and the OMB and everybody else who grinds numbers out in this place. We found out that we could not get any good numbers. We understand, it would probably impact the trust fund $5 billion, but the paybacks or the offsets as far as FICA taxes are paid in and income taxes that are paid in in those areas, would reduce the cost of about $2.9 billion.

The information and the testimony that we have had in our task force hearings while studying this issue for a period of time, found that there is a dynamic out there that you can measure. You know how many people are working now. And when you repeal the earnings test, you know how many people are going to be affected. But I brought this bill and this issue, along with my colleagues before the Congress because, in my experience in going back home and dealing with people week in and week out in town meetings and personal meetings, just everyday contact with your constituents, time and time again, week in, week out, we have had brought before us the situations of people who, in good faith, have been working since the 1930's. They really believe that the $10,000 or $8,000 or $6,000 benefit they receive when they retired was a bonanza. Of course, this is what they made their plans on, and this is what they built their future on.

Today, when a recipient receives $8,000 or $10,000 in Social Security benefits, he or she is struggling to survive. Let me give you a couple of examples of people that I have encountered.

One widow, 67 years of age, who lives in my district, and works in a flower shop, earns just above the minimum wage, $4.50, $4.60 an hour. When she makes $8,800, she quits because she does not want to jeopardize her future earnings. But as she relates, she has a daughter that is going through graduate school. She has payments on a home. She had to buy a new car a couple of years ago because the car that her husband left her 5 years ago just did not work any more. And from time to time, she likes to do a few things that other senior citizens do and have the ability to do.

Her friends are not impacted by this because their income is not earned income. Their income is unearned income. They get money from annuities and pension funds and savings accounts and moving their money around in CD's and other interest bearing accounts. She never had that luxury to do that. She feels that here is a class of people who have unearned income. They are not impacted by the law. But yet somebody who works and makes a living and has to make a living to survive today is impacted because she is working from the sweat of her brow and really does not think it is fair.

Another gentleman that I have talked to several times in my visits back to the district is a laborer. He has been a laborer all his life. He paid in to Social Security all his life. But he is part of an underground economy, a sub rosa economy, and he is one of many, I am sorry to say, in my district who live that way. They take money under the table. They are working as cement finishers, contractors and farm help. They are also working in stores as clerks. We are forcing a whole class of people to become criminals, in a sense, because this inequity that exists.

The practical side of this thing is that we are taxing people out of the work force, which I do not think was the intent of the earnings limit. I think times have changed, and certainly our discussion with Mr. Armey and, before that, the esteemed ranking member on Ways and Means, we are looking at a moving target. Things have changed over the years. Those dollar targets and earnings targets have moved, and they are going to move again next year.

I think it is only fair, that people being able to continue earning and being productive, and not being taxed out of the work force because somebody reaches—I think the number is $4.63 an hour. And if he goes above that $4.63 an hour, which is a very minimum wage, that if he goes 10 cents or 15 cents above that all of a sudden he reaches a marginal tax rate of 83 percent when you add in all the other taxes that he has to pay.

It is not really a fair situation. I think there are a lot of people in this country—and I am talking about hundreds of thousands of people—that want to be productive, that want to make a contribution, that want to improve their lifestyle, and they really do not understand all the nuances of the law, whether this is an entitlement or whether this is insurance and the discussions we have had before. But they want to contribute. They want to make their life better, and they want to make it better for their kids and themselves.

When we open the opportunity for people to go to work, they pay income taxes, State income taxes; they are paying FICA taxes into the program. Also, most of them move into a private insurance situation. They are not under the umbrella of Medicaid any more.

And certainly that is a positive thing. We are trying to get some independent groups out there, some think tanks, to put their pencils to paper and try to come up with some numbers.

I really appreciate coming before you today and being able to discuss this. It is an issue that certainly is nerve tips to senior citizens. I would like to be able to answer any questions if you might have some.

[The statement of Mr. Hastert follows:]

TESTIMONY OF

CONGRESSMAN J. DENNIS HASTERT

May 25, 1989

Before the House Ways and Means

Subcommittee on Social Security

Mr. Chairman and fellow colleagues on the Subcommittee, I want to thank you for the opportunity to testify before the House Ways and Means Subcommittee on Social Security on an issue of paramount importance to our nation's older Americans, the Social Security Earnings Test.

As you know, the earnings test is a provision in the law that reduces Social Security benefits $1 for every $2 recipients earn in outside income beyond a threshold, which is currently $8,880 for those aged 65-69 and $6,480 for those aged 62-64.

This month of May, declared by Congress as Older Americans Month, has been an historic one for the millions of senior citizens in this nation who hope for fundamental change in the Social Security Earnings Test.

First, in the Senate, Mr. Armstrong overwhelmingly passed amendments to both the minimum wage bill and budget resolution that would greatly liberalize the earnings test, a strong expression of support for change. The fact that the two amendments were removed in conference committee did not silence the debate.

Second, last Thursday the Republican Research Committee held hearings on the Social Security Earnings Test. As Chairman of the Task Force on the Social Security Earnings Test, I presided over those hearings. It was a spirited discussion, sometimes heated, over the merits of the issue. Testimony was given by a wide variety of respected individuals from Robert Myers, former Chief Actuary of the Social Security Administration to Stephen Moore, economist at the Heritage Foundation.

Third, just yesterday, I stood with some of my colleagues outside the Capitol to announce before the media and for all the country to consider, a bill which would repeal the earnings test for those at the normal retirement age and above, namely, aged 65 and over. The language of the bill is not unlike what you have seen before, Mr. Chairman. Bills to repeal the earnings test have been introduced in numerous sessions of Congress.

What's different about this bill is the number of cosponsors. I have signed on more than 115 of my fellow colleagues as original cosponsors--representing the first time ever that a bill to repeal the Social Security Earnings Test has broken the 100 cosponsor level.

Clearly, a new breeze is blowing in Congress. Mr. Chairman, I commend you for your foresight on this issue by holding hearings on revising the earnings test on Social Security.

Let me now focus my thoughts on the issue at hand.

The Social Security Earnings Test is a provision as old as Social Security itself. The earnings test was a part of the landmark Social Security Act of 1935. But before the system paid out its first benefit in 1940, the earnings test was changed in 1939. It was to be a portent of things to come. Congress has seen fit to change the earnings test in some fashion sixteen different times, most recently in 1983.

Most of the changes were made to either increase the threshold of when the test begins, or reduce the amount of Social Security benefits lost as a result of working beyond the threshold.

While I applaud these efforts at liberalizing the earnings test, they did not address the whole problem--those changes only limited its scope. My bill, the Older Americans Freedom to Work Act, would correct the problem, once and for all.

The underlying problem is the oppressive tax burden we have shouldered on our nation's older Americans that has made a whole class of citizens feel unwanted in the workforce.

The Social Security Earnings Test alone, saddles them with an effective 50% marginal tax rate, a rate I dare say is not paid by the Donald Trumps and Lee Iacoccas of the nation. We are thus sending a thundering message to our seniors to stay home, don't work, don't be productive members of our society.

Unfortunately, there are a few other "senior only" taxes, including the new catastrophic surcharge and the tax on Social Security benefits. When these are combined with the taxes all of us pay when we work such as federal and state income taxes, as well as FICA taxes, senior citizens are effectively taxed at a marginal rate in excess of 80% for each additional dollar they earn.

Senior citizens respond the same way we all would under similar circumstances--they "just say no." Today, 83% of all men and 92% of all women age 65 and over are completely retired. Between 1970 and 1985, the retirement rate among those 65 years old has increased a staggering 40%.

This statistic should be alarming to us all, for the real loss goes much deeper than the numbers--83% of men and 92% of women aged 65 and over retired. The real loss is the invaluable experience and knowledge that older Americans can pass on to succeeding generations in the workforce. This loss cannot be calculated by the brightest CPAs in the world.

Repeal of the earnings test would not only send the right signal to older Americans that we value their work, but it would also relieve the current squeeze in the labor market.

The U.S. Labor Department has warned of shortages in the labor market. There's good reason to believe that this labor shortage is more than just cyclical. Factors contributing to a labor shortage well into the 1990s include a tightening immigration policy, low fertility rates and the baby boom generation having fully entered the labor market.

Aldona Robbins, Vice President of Fiscal Associates, Inc., and former senior economist the the U.S. Treasury Department, estimates that between 300,000 and 600,000 older workers would re-enter the labor force or increase their work effort as a result of repealing the earnings test.

Some naysayers agree with the logic behind repealing the earnings test, but argue that it would be too costly to the Social Security Trust Fund and so shouldn't be attempted. In other words, they agree repealing the earnings test is the "right thing to do," but say we can't afford it.

About the only thing everyone is able to agree on is that no one has the final say on just how much revenue would be offset by an induced work effort. I implore the Subcommittee to research this issue to the fullest extent possible.

Some economists have estimated a revenue offset by an induced work effort from one-third and two-thirds of the higher Social Security benefit outlays. The current cost of our bill, estimated recently by the SSA, would be an average of $5.25 billion annually over the next ten years. A revenue offset of one-third to two-thirds would mean a cost to the trust fund of between $1.75 and $3.5 billion annually.

Finally, let me address one other obstacle to repeal of the earnings test. It's been said by some that repeal would only help wealthy older Americans, that the middle and lower income senior would largely be unaffected. Nothing could be further from the truth!

Take an example of one of the senior citizens back in your district who works full-time at the local grocery store to supplement his Social Security check. If he or she is making $4.63 an hour, he has already confronted the earnings test threshold. In other words, if he chose to work beyond that point, he would lose $1 in his check for every $2 he earns thereafter.

Clearly nobody believes that anyone making $5, $6 or $7 an hour is part of any elite class. Yet these are the very people who are hurt most by the earnings test.

Another important fact to keep in mind is that the test is an EARNINGS limit, not an INCOME limit. Unearned income is not subject to the earnings test. Think for a minute about all the different types of unearned income not subject to the earnings test--pensions, dividends, interest, investments and inheritances. Now think of the income group that profits most from these--that's right the wealthy.

It would not be difficult to come up with situations where a wealthy senior is completely retired and living on a pension and investment income exceeding say, $50,000. He would not have to worry about losing one penny of his Social Security check. Meanwhile, the frugal senior citizen who works at the local grocery store making $4.63 an hour will start to lose $1 for every $2 he earns above and beyond his normal work schedule until his whole Social Security check is depleted.

The end result is that the earnings test penalizes low and middle income retirees for working while ensuring a tax-sheltered bonus for those who can afford to withdraw from the labor force at 65.

Clearly, this example demonstrates that repeal is not for the wealthy. Its roots are as deep as the blue-collar work ethic itself.

Let me conclude by saying that I believe the Subcommittee has a golden opportunity to breathe new life into an old, but persistent issue. By advancing legislation to repeal the earnings test you will be advancing the cause for millions of senior citizens in America. In one fell swoop, we can together correct the root problem that Congress has addressed so many times. As the San Diego Tribune said in its endorsement of repeal, "We think it is time that the law, not the older workers, be retired."

I thank you, Mr. Chairman, for the opportunity to appear before the Subcommittee on Social Security and would entertain any questions you may have.

Chairman JACOBS. Mr. Brown.

Mr. BROWN. I would just like to commend the gentleman for his leadership in this area. I agree with you. I think it is a prime concern of many of our senior citizens.

Let me ask on the insurance aspect, are you saying that encouraging more people to work in this area, or allowing them to work by eliminating the penalty, would have a significant impact on reducing the cost of the Medicare Program as well?

Mr. HASTERT. Right, because our preliminary investigations show that people will go to work, many who stopped working at age 65. They are in the private work force and covered by group insurance. They move out of the Medicare umbrella.

Mr. BROWN. So if they have private insurance, it is primary coverage, and Medicare only covers that which may not be covered by that insurance?

Mr. HASTERT. Right. Exactly.

Mr. BROWN. Do you have any estimates at this point?

Mr. HASTERT. We are trying to get them. Again, we are working on the edge of fuzz in here in trying to get hard numbers, because we are limited in making some of those projections. But we do have several groups that are trying to grind out those numbers so that we have something substantial to give to you.

Mr. BROWN. Thank you.

Chairman JACOBS. We thank you, Mr. Hastert, for your contribution to the record.

I think I might say for the record now, a statistic that Ms. Dorcas Hardy worked up a couple of years ago in terms of what people contributed and what they are getting from Social Security—I believe that she said that at the bottom of the notch years, after things were almost back to what they were intended to be when the 1972 cost of living element was inserted into the Social Security Program, that the person who had—the man who had worked and paid the maximum Social Security tax during his working years and had a spouse who was not in covered employment, who retired, as I say, in 1987, would receive everything paid in, plus interest at T bill rates, within 3⅓ years, and for the rest of the 16-year life expectancy, on the average. You could call it nothing else, generically, than a subsidy from the people who are paying Social Security taxes now.

So on your point that people didn't anticipate how little $8,000 might be, I would just point out that by comparison with other retirement programs, it is quite, quite rare that a private pension plan pays any kind of cost of living adjustments.

Mr. HASTERT. It is an interesting point that you bring up, and it is something that we have been confronted with when meeting with senior citizens because we find, for instance, the gentleman who retires and his wife has been a teacher, for instance, they have counted on that teacher income, pension income. All of a sudden, their income is adjusted down, and not as a supplement.

Chairman JACOBS. Yes. It will be offset because of the——

Mr. HASTERT. Right.

Chairman JACOBS. Our colleague, Bill Archer, once ran aground with Phyllis Shlafly. She was here to testify, and he said in the purist logic the spousal benefit is welfare, because it is a benefit that goes 50 percent beyond what the worker earned.

And as I recall, Ms. Shlafly went down and ran radio ads in Bill's next election, and I think he was knocked all the way down from 80 percent of the vote to 79.9 percent of the vote as a result.

So I just say that that itself is a generosity in the program. Now, you might say that the bachelor who pays in and never receives a spousal benefit for his family might stop being a bachelor one of these times, and happy that he had paid in. So I think there is an argument both ways on that.

The other thing our staff director handed me just now—they say out in Oklahoma, if you want to know what a cowboy will do when he gets drunk, you find out what he did the last time he got drunk.

In terms of what the economy did the last time there was a substantial liberalization of the retirement test, which happened in the 1970's, I am told that there was an imperceptible change of entry into the work force or greater number of hours worked in the economy.

So I think it is appropriate to put that statistic in.

Mr. HASTERT. There are two things I learned a long time ago, and I am a rookie around here, actually in my second term. I wouldn't want to run aground of Phyllis Shlafly, being from the Midwest, so I am going to be real careful, Mr. Chairman, of what I say, and wouldn't want to argue with this——

Chairman JACOBS. She is a very talented lady, except not so good in Texas elections, I guess.

Mr. HASTERT. I also want to say that we put this bill forward as generic as possible because there are ways of finding a solution. Phasing it in at a $20,000 or $25,000 threshold, also, in the outyears makes this almost revenue neutral. And so we did that to—if you have your opportunity, and we certainly hope you do, you can work your will upon this piece of legislation, too.

Thank you very much.

Chairman JACOBS. Unfortunately, we have to live in the in-years, also. But thank you very much for your contribution.

Mr. HASTERT. Thank you for the opportunity.

Chairman JACOBS. Let us see. I guess—oh, sure, Mr. Houghton is our next contributor. As a Member of Congress, you are very definitely a contributor to the Social Security System.

STATEMENT OF HON. AMO HOUGHTON, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF NEW YORK

Mr. HOUGHTON. Well, Mr. Chairman, Mr. Brown, thank you very much for letting me be here today. I have written testimony and, blessedly, I will not read it, but what I would like to do is to hit just a couple of the high points to give you a little bit of a feel for what I think are the important issues, and also maybe the background.

I have proposed and submitted a bill the first day of Congress, H.R. 190, which is self-explanatory, and I think you have a copy of this. But the basic argument of the bill is that the earnings provision is no longer applicable. In other words, it is a one-time purpose which is changed with the years. And, second, the needs of this country require that it be changed.

A variety of different things, as you know, have taken place. There is a lower birth rate; there is a lower skill bank. We have an extraordinarily continuous—slow, but continuous growth rate, and there is a much freer flow of goods back and forth in this world than there was.

The basic point, I suppose, is this: In the past years, the economic cycles usually come to an end because our economy runs out of capacity. Shortages occur, prices go up, consumers resist, sales and volumes go down, and a recession occurs.

Now, this will happen in some way and at some point again in the future. But my feeling is this, that because of the extraordinary quality programs which have been involved in American industry—financial restructuring, foreign sourcing, and the modest and not overheated growth rate—when the capacity point comes, it will not come because of the traditional shortage of equipment and buildings. It will come because of the shortage of skills and of skilled people.

Skills, as you know, are learned; they are valuable. It takes many years to provide the_skills for a manager or an individual contributor in a business, and people are living longer and staying healthy longer and it kills me to see people who want to work not working and who are needed to work, particularly in light of the trade deficit. We want to close it; it is important.

The country cannot afford, really, an operating deficit and a trade deficit. It has a cash problem. But to do this, we must produce products and not just services. Our productivity is coming along well, but it cannot take up the slack. We must have people. There is a large pool out there, and I would suggest that we use them.

Now, I realize that there is always a worry about the cost, and it probably will cost more. I am a little bit from Missouri on some of the figures which I read, whether it is 1 billion or 2 billion or 3 billion or 5 billion, if you eliminate this earnings test after the age of 65.

But all I know is that senior citizens, in general, work. They pay taxes, they spend. There is a cash flow going into the economy which they represent. And basically when somebody works, the Government saves money, whether it is in cash or whether it is in costs or whether it is an infusion of tax money. It is better off for the citizenry of this country.

So, Mr. Chairman, I thank you very much for letting me be here. I submit my written testimony, and that is it.

[The statement of Mr. Houghton follows:]

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TESTIMONY BY AMO HOUGHTON BEFORE HOUSE WAYS AND MEANS SUBCOMMITTEE ON SOCIAL SECURITY--THURSDAY, MAY 25, 1989

GOOD MORNING, MR. CHAIRMAN AND MEMBERS OF THE SUBCOMMITTEE. I've come here today to talk about an issue of great importance to me, to you, to our Nation. The issue is whether we are willing to help financially senior citizens, whether we will consider adjusting out of date infringements on their earning power and dignity.

On the first day of the 101st Congress I introduced H.R. 190. In a nutshell, this bill seeks to repeal the social security earnings limitation at age 65.

Social security was started before World War II--in the 30's. At that time, it seemed appropriate to install incentives for older workers to leave the work force--the point being--to open up jobs for others. Unemployment was reaching 25 percent.

Today of course we face a far different economic scenario. For example, by 1999 the Department of Labor estimates there will be 15 million fewer people between the ages of 18 and 25. Our capacity limitations in the next year or two will be reached not because of lack of plant and equipment. The limitation will be people. We need new sources of labor. This is where H.R. 190 enters the picture.

Now with all the humility I can muster, I personally believe that seniors can be a valuable new resource to business. In general with life expectancy rising yearly, these individuals over the "normal" retirement age are experienced and wise. They bring more to an organization than just a willingness to work. Yet we seem not to encourage them to work. As a matter of fact, it is quite the opposite. We tell them, "If you want to continue to be productive--to work, to earn money, to pay taxes--we're going to reduce the social security payment you're entitled to." So I ask--why punish these loyal, necessary people at a time when industry clamors for just the sort of skills they provide? Senior citizens who want to work should be encouraged. I'd like to believe my bill is a step in the right direction.

If I could hold my argument for just a moment, I remember sitting in the stands during President Bush's Inaugural Address. In it he said, "We must bring in the generations, harnessing the unused talent of the elderly...." Now, being a senior citizen myself, isn't a good way for him and for us to suit action to the word and harness the useful, but unused, pool of talent by repealing the social security earnings limit? It's that simple.

The argument goes that by repealing the earnings limitation, we would further increase our already out of control deficit. I've heard estimates of up to $5 billion. I don't believe them. I have no sense of how they were calculated. I frankly think that the actual cost is far less and the benefits would far outweigh any risk associated with this policy change. Seniors earn money. It is taxed. Seniors spend money, they help create new jobs. This new money will flow directly into the economy. The effects are real.

In addition, of course, repealing the earnings limitation at age 65 enables us to reduce, forever, a substantial cost associated with the social security program. The earnings limitation is an administrative nightmare. The Social Security Administration spends more than $200 million a year and uses 8 percent of its employees to police the income levels of beneficiaries. We can save these costs and more.

The bottom line, as I see it, is that the earnings test damages the economy. It is unfair to seniors. I think it's high time we repeal it.

Chairman JACOBS. Mr. Houghton, we are grateful both for your testimony and the conciseness of it at this hour. Thank you very much.

Mr. HOUGHTON. Thank you very much.

Chairman JACOBS. John Rhodes, a famous name around here.

STATEMENT OF HON. JOHN J. RHODES III, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF ARIZONA

Mr. RHODES. Mr. Chairman, as far as conciseness is concerned, you haven't seen anything yet.

Chairman JACOBS. Your father reared you well.

Mr. RHODES. Thank you, sir. One of the things you learn is that the juniorest will be the lastest and, in that position, by the time you get there everything that you wanted to say has been said at least three times.

Chairman JACOBS. I think it is alphabetical, by the way.

Mr. RHODES. My written statement is in the record. It has nothing new in it. I have a summary of my written statement; it has nothing new in it. I have no anecdotal experiences to relate that are spectacularly different from anything that you have heard so far.

I am going to say words that I have prayed to hear when I have been sitting in your position, which is I have nothing further to say. Do you have any questions?

[The statement of Mr. Rhodes follows:]

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STATEMENT
OF
CONGRESSMAN JOHN J. RHODES, III

May 25, 1989

Before the Subcommittee on Social Security

I want to thank Chairman Andy Jacobs for providing me the opportunity to testify on this issue, which is so vital to American Senior citizens.

The Social Security earnings test has been in existence since the payment of the first Social Security benefit. It has changed since 1940, but it is no less onerous to those persons affected by it.

Consider the origin of Social Security. Created during the Depression in 1935, Social Security sought to achieve two goals, moving older workers out of the work force to make way for younger workers and to partially replace lost income due to retirement. Those goals were applicable in 1935, but they are not applicable in 1989.

The original earnings test affected retired persons earning over $15. They suffered the loss of their entire Social Security benefit. Since then, the test has undergone a variety of changes. It became an annual test as opposed to monthly; the amount of earnings allowed has increased (currently it is $8,880); the amount of benefits lost has been decreased, (in 1990 the penalty will be $1 for every $3 earned over the limit), and finally, the Congress established of an exempt age of 70 years.

Many of us believe this is a sign that the test is antiquated, inefficient, draconian, and ripe for elimination. To be exact, there currently are 15 bills pending before Congress which would in some way significantly alter or eliminate the test. Over 128 members have signed on to these various measures.

Recent action taken by Senator Bill Armstrong forces all of us to consider the legitimacy of the test. Senator Armstrong attached an amendment to the minimum wage legislation, but House conferees insisted was non-germane, thus it was dropped. He also attached his earnings test language to the Budget Resolution. In that instance, the earnings test language was modified by language directing the House Ways and Means Committee and the Senate Finance Committee to do a study and determine the current tax situation of the elderly.

I believe the answer to the question posed in that language is already known---today's elderly are facing marginal tax rates that can be as high as 122 percent. We take pride in pointing out the lower numbers of impoverished elderly in America, but we seem to set out to punish those same persons who have been able to keep themselves out of poverty, by slapping them with exorbitant marginal tax rates.

Some argue that only the rich benefit from eliminating the earnings test. I question the legitimacy of that argument. Is it right for any individual to face tax rates of 65 percent? Is it fair to preclude any individual from continuing to earn their wages, without penalization, because it does not benefit his neighbor?

-more-

Consider also the current labor market in today's society. By the year 2030, there will be only two workers for every elderly citizen. The nation's labor market lacks skilled laborers because they are forced from the work force by the artificial penalties they could face if they continued to work. The Wall Street Journal reports that 83 percent of all men and 92 percent of all women over 65 are completely out of the work force. Three out of five of these do not have any disability that would preclude them from working. If these persons have retired voluntarily and do not wish to work, that is their right; but it is also the right of those persons who wish to continue working to do so without penalty.

The complexity of the current system must also come into question. It costs the Social Security Administration (SSA) over $200 million a year simply to administer the earnings test. The elderly must determine what their earnings will be for the upcoming year and report that figure to the SSA which then makes any adjustments to the Social Security benefit. If any underestimation or overestimation occurs, a lump sum payment or refund is made. And that is only the extent of the SSA involvement. It does not take into account the Internal Revenue Service or the tax accountant elderly citizens will likely employ to try to figure out the complex interplay of the unique tax situation they faced.

Finally, the argument is made that this constitutes a raid on the Social Security trust fund, that it costs too much and should not be tampered with in any way. I disagree. In fact, no one can agree on what the actual revenue impacts would be. Some claim the elimination of the earnings test for those of retirement age and above will result in outlays of $5 billion a year. This figure does not take into account the savings that can be estimated from decreased administrative expenses, and increased Old Age Survivors and Disability Insurance revenue as a result of taxation of benefits, and the increase work effort. Even this recoupment figure is subject to dispute. Depending upon the estimator and the methods that can be used to lessen the budgetary impact, such as the delayed retirement credit, recoupment figures have been judged to be as little as 10 percent and as much as 50 percent.

In closing, the question is not whether repeal is in keeping with the original intent of the Social Security system, it is not will repeal only benefit the rich; it is not what numbers of elderly will re-enter the workforce. The crucial question is whether the federal government should tell a Social Security recipient he or she cannot continue to be a productive wage earning citizen without being penalized for that initiative. My answer to that question is no.

Thank you.

Chairman **Jacobs**. Mr. Brown.

Mr. **Brown**. I want to commend the gentleman on an exciting and new statement. [Laughter.]

I thank him for his brevity.

Mr. **Rhodes**. Mr. Chairman, thank you very much for having these hearings. We all do appreciate that.

Chairman **Jacobs**. You might be setting a bad example for a man who aspires to be a Senator. My father says in that body there is free and unlimited coinage of words.

Thank you very much for your contribution.

Mr. **Rhodes**. Thank you, sir.

Chairman **Jacobs**. Let us see. Helen is not back. I think, Mr. Enoff, you are up to bat. Did you go home last night?

Mr. **Enoff**. I was wearing out the parkway, but——

Chairman **Jacobs**. Well, we may start charging you rent, but I don't think so. Go ahead.

STATEMENT OF LOUIS D. ENOFF, DEPUTY COMMISSIONER FOR PROGRAMS, SOCIAL SECURITY ADMINISTRATION

Mr. **Enoff**. Well, it is a pleasure to be here, Mr. Chairman and Mr. Brown, to discuss some of the provisions of the retirement earnings test. I, too, have submitted a statement for the record, but I would like to make a few points, maybe, in summarizing some of the things that have been said today, reiterating some of the points that have been raised in favor of eliminating, as well as those that would favor retaining, the earnings test.

We all know that the basic philosophy of the original program was that retirement benefits were intended to partially replace income lost due to retirement. The retirement earnings test was designed as an objective measure of the extent to which earnings are lost due to retirement.

Thus, a beneficiary who continues to work may lose some or all of his benefits under the test.

There has always been an earnings test, although it has changed quite a bit over time. The current earnings test reduces benefits by $1 for each $2 of earnings. The annual exempt amount for 1989, we have mentioned earlier, is $8,880 for those 65 to 69, and each year about 1.5 million persons lose some or all of their benefits as a result of the test.

Proponents of the test have generally made the following arguments: that eliminating the test would change Social Security from insurance against the loss of income to an earnings-based annuity; that eliminating the test would primarily advantage higher-income beneficiaries; that current law already provides for further liberalization of the test—that is, in 1990, the $1 for $2 benefit reduction rate goes to $1 for $3 for those aged 65 to 69; that eliminating the test would be costly—benefit payments could increase by about $11 billion per year under some of the elimination proposals; that eliminating the test would decrease the work incentive for some beneficiaries, since they could work less and still receive the same income; and that Social Security Program rests on the policies developed by the bipartisan National Commission on Social Security Reform in 1983.

On the other hand, those in favor of modifying or eliminating the test have generally used the following arguments to support their position. Social Security benefits are an earned right, bought and paid for, and should not be withheld from eligible beneficiaries for any reason. The earnings test is a form of needs test which is inappropriate for this earned-right program. And the annuity concept has already been established, since benefits are payable in full at age 70, regardless of earnings.

They also have stated that the test discourages beneficiaries from working because of the effective marginal tax rate that you have heard about today, and that it approaches 100 percent. Also, that by discouraging beneficiaries from working, the test deprives the country's labor force of the valuable skills of older workers.

The test also encourages older workers to participate in the underground economy. The test discriminates against those who depend on income from work rather than on investment income to supplement their benefits.

The cost of eliminating the earnings test could be offset in part by additional Social Security taxes and income taxes attributable to increased labor force participation. Finally, the test is complicated, difficult to understand, and costly to administer. As has been stated earlier, elimination of the test at age 65 could save the Social Security Administration about 2,500 work-years per year.

We in the Social Security Administration are currently examining the effects of the earnings test on labor force participation of the elderly. We will continue to do that, and we stand ready to work with this committee in exploring alternatives.

I would be pleased to answer any questions which you may have today.

[The statement of Mr. Enoff follows:]

Statement of Louis D. Enhoff, Deputy Commissioner for Programs, Social Security Administration

Mr. Chairman, I am pleased to appear before you today to discuss the Social Security retirement earnings test.

I will start by giving a brief history of the test and a *description of how it works* **today. Then I will discuss the pros and cons of retaining the test.**

HISTORY OF THE TEST

The basic philosophy of the original Social Security program was that Social Security retirement benefits were intended to partially replace income lost due to retirement. The retirement earnings test was designed as an objective measure of the extent to which income is lost due to retirement. Thus, under the test, a beneficiary who continues to work after becoming entitled to Social Security benefits may lose some or all of his benefits, depending on his annual earnings.

The Social Security program has always had an earnings test, although it has changed quite a bit over the years. When benefits first became payable in 1940, a beneficiary lost his entire benefit for any month in which he earned $15 or more in covered earnings. The earnings test has been modified many times since then to:

- Convert the monthly test to an annual test;
- Broaden the scope of earnings countable under the test;
- Increase the amount of earnings that a beneficiary may earn without losing any benefits;
- Provide for a gradual reduction of benefits as earnings levels increase; and
- Establish an age at which beneficiaries are exempt from the test.

HOW THE CURRENT TEST WORKS

The earnings test reduces benefits by $1 for each $2 of earnings above the annual exempt amount. The annual exempt amount for 1989 is $6,480 for beneficiaries under age 65 and $8,880 for beneficiaries age 65 to age 69. Beginning with 1990, beneficiaries age 65 to age 69 will lose $1 for each $3 of earnings above the annual exempt amount. These exempt amounts are adjusted annually to reflect increases in average wages. Workers are exempt from the test when they reach age 70. The test does not apply to disability beneficiaries, who are subject instead to a substantial gainful activity test, but it does apply to dependents of disability beneficiaries.

A worker's earnings above the exempt amount affect not only his own benefits, but also the benefits of family members receiving benefits on his earnings record. The earnings of a dependent or survivor beneficiary can affect only that beneficiary's benefits.

Each year, about 1.4 million persons lose some or all of their benefits as a result of the test. Of this group, about 935,000 are beneficiaries who lose benefits because the test is in effect from age 65 to 69. This includes retired-worker beneficiaries age 65 to 69, dependents of any age receiving benefits on the same record, or survivors age 65 to 69. About 140,000 persons do not file for benefits because the RET is in effect from age 65 to 69. About 515,000 other beneficiaries also lose some or all of their benefits. These are workers, dependents, and survivors under age 65.

ARGUMENTS FOR RETAINING THE EARNINGS TEST

Proponents of the test have generally presented the following arguments whenever the issue of eliminating the test has been raised:

- Eliminating the test would change the Social Security retirement program from insurance against the loss of income at retirement to an earnings based annuity payable upon reaching a defined retirement age.
- Eliminating the test would primarily advantage higher income beneficiaries because the current test affects the benefits of high earners to a greater extent than low earners.
- Current law already provides for further liberalization of the test. In 1990, the $1 for $2 benefit withholding rate above the annual exempt amount will be $1 for $3 for beneficiaries age 65 to 69.
- The test holds down program costs. If the test were entirely eliminated immediately, benefit payments could increase by about $11 billion per year.
- Eliminating the test would decrease the work incentive for some currently working beneficiaries now affected by the test since they could work less for the same amount of total income.

ARGUMENTS FOR ELIMINATING THE EARNINGS TEST

Those in favor of modifying or eliminating the earnings test have generally used the following arguments to support their position:

- Social Security benefits are an earned right--bought and paid for--and should not be withheld from eligible beneficiaries for any reason. The earnings test is a form of needs test which is inappropriate for an earned right program. Further, the annuity concept has already been established at age 70 since benefits are payable at that point regardless of earnings.
- The test discourages beneficiaries from working because the effective marginal tax rate on earnings--taking into account the test itself, Social Security taxes, and Federal, State, and local income taxes--can approach 100 percent.
- By discouraging beneficiaries from working, the test deprives the country's labor force of the valuable skills and experience of older workers. As labor force growth slows, there will be labor shortages, and there is a need to encourage older people to participate in the labor force.
- The test encourages older workers to participate in the underground economy, especially those who are most in need of additional income.
- The test discriminates against those who depend on income from work rather than on investment income to supplement their benefits. Beneficiaries who have unearned sources of income--generally those at higher earnings levels--can receive their benefits without penalty.
- The cost of eliminating the test would be offset in part by additional Social Security taxes and income taxes attributable to increased labor force participation by older workers.

- The test is complicated, difficult to understand, and costly to administer. Elimination of the test could save about 2,500 workyears.

CONCLUSION

The Social Security program rests on the policies developed by the bipartisan National Commission on Social Security Reform and enacted in the Social Security Amendments of 1983. The Commission unanimously recommended that Congress "not alter the fundamental structure of the Social Security program or undermine its fundamental principles."

I have explained the arguments for eliminating the retirement earnings test. However, eliminating the earnings test now would cost the trust funds billions and would turn us away from the major policies adopted by the 1983 Commission and approved by the President and the Congress. The Social Security Administration is examining the effects of the earnings test on labor force participation of the elderly along with other critical issues affecting the retirement security of America's workers.

Chairman **Jacobs**. Mr. Brown.

Mr. **Brown**. Thank you, Mr. Chairman.

It is Mr. Enoff?

Mr. **Enoff**. Yes, sir.

Mr. **Brown**. You mentioned there were about 1.5 million folks who currently pay this penalty. Tell me, do you have a feel for how that breaks down of those over 65 versus those under 65?

Mr. **Enoff**. Yes, sir; 935,000 beneficiaries, 65 to 69; 770,000 of those would be workers, 125,000 dependents, and 40,000 would be survivors. In addition, 140,000 persons do not file for benefits because of the retirement earnings test in that category. So you have to add the 140,000 to the 935,000 and I guess that puts you at 1,075,000, if my math is correct.

The other 500,000 or so would be those aged 62 to 64.

I can supply you the full breakdown.

Mr. **Brown**. So you are saying somewhere in the neighborhood of 300,000 to 400,000 in the under 60——

Mr. **Enoff**. Under 65. These totals add to 500,000. Somehow, 935,000 and 140,000 doesn't seem to add, does it? There must be a netting effect. Let me give you the breakdown, but 400,000 to 500,000 has got to be the number.

Mr. **Brown**. Do you have a feel for how much of the $11 billion penalty or benefit increases that would result if you repeal this would accrue or would be paid by those under 65 versus those over 65?

We have seen estimates of something in the neighborhood of $5 to $6 billion being attributable to the portion of the population over 65.

Mr. **Enoff**. I would think it would certainly be the majority, based on the numbers and the fact that the earnings tests would prevent many from working at all at that point, while those under 65 would simply not retire.

I can give you that breakdown. I do not have it at hand, but we would be pleased to give it to you.

Mr. **Brown**. Do you have a feel for what would be generated in income if we eliminated the base that people under 65 are currently allowed to earn without paying the penalty; that is, the $6,480 a year that they are not currently allowed to generate without having a forfeiture?

Mr. **Enoff**. If we eliminated the test for those under 65?

Mr. **Brown**. Well, no; if we simply said that there is no exempt amount that you can earn first before the penalty applies.

Mr. **Enoff**. I see. So you are saying that there would be a full penalty, in effect?

Mr. **Brown**. Full penalty, and I guess where I am headed is does that generate enough in a static analysis to offset the elimination of the penalty for those over 65?

Mr. **Enoff**. I don't believe it does offset it completely. But, again, I would supply that estimate. I am sure we would have that.

Mr. **Brown**. I think that would be most helpful for the committee——

Mr. **Enoff**. Sure.

Mr. **Brown** [continuing]. Because, obviously, to sell this to the majority of the committee, we need to figure out a way to pay for it that they are comfortable with.

Mr. **Enoff**. I would be pleased to supply that. One of the problems we run into here—and you have heard criticisms of the estimates—is that we are estimating something that really has never quite occurred before if you eliminate the test.

Mr. **Brown**. Sure.

Mr. **Enoff**. And I think the same thing would be true, but we would be glad to give you those figures, and those should be easily obtainable.

Mr. **Brown**. Tell me—the suggestions here today that there are major offsets in revenue in terms of additional work being performed, additional Federal taxes being paid, additional Social Security revenue, additional State taxes, lower Medicare costs—do we have estimates in that area at this point?

Mr. **Enoff**. The estimates that we have, Mr. Brown—our actuaries have looked at this, together with the revenue estimators from the Treasury Department, and we come up with about a 10-percent offset of the costs as a result of those additional revenues.

That has been criticized by some as being too conservative, and we would be pleased to see other data. But as of this point, that is the only number that we have to come up with a reasonably accurate estimate. I have heard some say today that they are having others look, and I have heard recently of some, but I haven't seen any that have the data behind them that would enable us to go any further.

Mr. **Brown**. Well, help me understand that. That does not include State taxes or Medicare?

Mr. **Enoff**. It does include some estimate of Medicare, which is estimated to be not a substantial amount. One of the items is an offset based on an assumption that some persons want a certain income level, and therefore, if they would receive more in benefits, they would lessen the amount of work they do. That offsets the savings.

Mr. **Brown**. What kind of change in behavior do you use for those estimates?

Mr. **Enoff**. I can give you the assumptions. I don't have all of them here, but as I say, there is an estimate of that certain percentage of persons and we would be glad to have our actuaries sit down and go through it. That is one of the difficulties. We are estimating behavior that there is no precedent for estimating. I will be very frank about that.

I think we have to go with what we know, and we cannot estimate certain———

Mr. **Brown**. Well, I think the subject of semistatic analysis is one that has been long debated and, of course, we won't resolve today. But just for background information, these are estimates that the Social Security Administration has done, not necessarily OMB or CBO?

Mr. **Enoff**. We did compare and use Treasury's revenue estimate. Treasury is in the revenue-estimating business, but we have applied it to the Social Security population.

Mr. **Brown**. Basic assumptions in terms of behavior modification—those were done by whom?

Mr. **Enoff**. By us. Social Security's assumptions are used here, and I think we have looked at the literature and what there is available, little as it is, to come up with that estimate.

Mr. **Brown**. Thank you. Well, we would appreciate anything you can supply us in these areas.

Mr. **Enoff**. I will supply those, and we would be pleased, as I say, to work with the committee in exploring this area.

Mr. **Brown**. Thank you.

Chairman **Jacobs**. Mr. Enoff, one question. The information I was handed by the staff and repeated for the record a moment ago about the effect on the participation in the labor market by liberalization of the retirement test—will you confirm what was said?

Mr. **Enoff**. Were you talking about going from age 72 to 70? I wasn't sure what you were referring to there. When the earnings test was lowered from 72 to 70, the increase in dollars, the one-for-two rather than——

Chairman **Jacobs**. I thought that is what was meant. The increase in the dollar limits didn't result in much greater participation in the job market. Do you have any information on that?

Mr. **Enoff**. I wouldn't have—I certainly assume that the estimates would be consistent with what we have said. As I say, the issue, though, is, I think, whether this is the same kind of a change in the test, and I don't know that we can——

Chairman **Jacobs**. To the extent that it were comparable—that is to say, the same real dollars—we might make some inference.

Mr. **Enoff**. Sure.

Chairman **Jacobs**. So, as you leave now for lunch, you might bear that in mind, too, and give us a little note on that.

Mr. **Enoff**. OK. I will be glad to look at what we do have on that. As I say, the change was—I think originally it was age 75 and then it went to 72 and then age 70, and, of course, the $1 for $2 and now $1 for $3 proposal.

We will be glad to supply anything we can and to estimate with you as you go through this.

[The following was subsequently received:]

On May 25, 1989, the Subcommittee on Social Security of the Committee on Ways and Means held a hearing on the subject of the Social Security retirement test. During the hearing several questions were asked which could not be fully answered by the Social Security Administration's representatives. Following is a restatement of these questions:

> 1) Of the 1.4 million social security beneficiaries affected by the retirement test, how many are age 65-69, and how many are under age 65? Within each age group, how many receive retirement benefits (broken down by sex), dependent benefits, and survivor benefits? If the test were eliminated, how much of the newly payable benefits would be paid to persons age 65-69, and how much would be paid to those under age 65?
>
> 2) If the exempt amount of earnings for those under age 65 were set at zero, what would be the savings to the trust funds? Would it offset the cost of eliminating the retirement test for those age 65-69 (assuming no change in retirement behavior or labor force participation)?
>
> 3) What is the estimate of the amount of additional revenues and lower medicare costs that would result if: a) the exempt amount were raised by $1,040 in 1990; b) the exempt amount were raised in $3,000 increments in 1990, 1991, and 1992; and c) the retirement test were repealed altogether at age 65? What assumptions do these estimates use regarding behavior changes in response to a change in the retirement test?
>
> 4) In 1972, the retirement test was liberalized when the dollar-for-dollar withholding rate was changed to a rate of $1 of benefits withheld for every $2 of earnings over the exempt amount. In 1977, the test was substantially liberalized when the exempt amount was increased by $1,000 in 1978 and by increments of $500 in each of the next four years. What was the response of the labor force to these liberalizations? How does the value in real dollars of these increases in the exempt amount compare with the value in real dollars of some of the most recent proposals to raise the exempt amount -- namely, increasing the threshold by $1,040 in 1990, or increasing it in $3,000 increments for three years?

Prepared by the Staff of the
Subcommittee on Social Security

1. Of the 1.4 million social security beneficiaries affected by the retirement test, how many are age 65-69, and how many are under age 65? Within each age group, how many receive retirement benefits (broken down by sex), dependent benefits, and survivor benefits? If the test were eliminated, how much of the newly payable benefits would be paid to persons age 65-69, and how much would be paid to those under age 65?

In 1990, about 1.5 million beneficiaries are expected to lose some or all of their benefits as a result of the earnings test.

- About 935,000 beneficiaries lose benefits because the test is in effect from age 65 to 69. This includes 770,000 retired-worker beneficiaries age 65 to 69 (530,000 male and 240,000 female), 125,000 dependents (of any age) receiving benefits on the same earnings record, and 40,000 survivors and dependents age 65 to 69 who lose benefits because of their own work.

- About 525,000 beneficiaries lose benefits because the test is in effect for persons under age 65. This includes 180,000 retired-worker beneficiaries age 62-64 (105,000 male and 75,000 female), 25,000 dependents (of any age) receiving benefits on the same earnings record, and 320,000 survivors and dependents under age 65 who lose benefits because of their own work.

In addition to the 1.5 million beneficiaries above, we estimate that about 100,000 persons do not file for benefits because the test is in effect from age 65 to 69 and about 1.1 million persons because the test is in effect for persons under age 65.

If the earnings test were completely eliminated beginning in calendar year 1990, additional benefits would be paid as follows:

Fiscal Year	Additional Benefits (In billions)	
	Age 65-69	Under Age 65
1990	$3.5	$5.1
1991	5.3	7.6
1992	5.4	7.5
1993	5.5	7.3
1994	5.6	7.2
Total	25.3	34.7

2. If the exempt amount of earnings for those under age 65 were set at zero, what would be the savings to the trust funds? Would it offset the cost of eliminating the retirement test for those age 65-69 (assuming no change in retirement behavior or labor force participation)?

If the annual exempt amount for persons under age 65 were set at zero, benefit outgo would be reduced by about $600 million annually. This savings would not offset the additional benefits which would be paid if the test were eliminated for persons age 65-69--estimated at about $5 billion annually.

3. What is the estimate of the amount of additional revenues and lower medicare costs that would result if the retirement test were repealed altogether at age 65? What assumptions do these estimates use regarding behavior changes in response to a change in the retirement test? (The question has been revised as subsequently directed by subcommittee staff.)

If the retirement earnings test were eliminated at age 65 in 1990, the increased revenues for the first 5 years (FY 1990-94) would be $1.8 billion due to the Federal income taxation of benefits and $.6 billion due to increased OASDHI payroll taxes. The reduction in Medicare costs over the same 5-year period would be $0.1 billion. (See attached chart.)

These estimates are based on the following assumptions concerning behavioral changes:

- 67,000 individuals would return to work;
- 220,000 workers would increase their earnings; and
- 376,000 workers would decrease their earnings.

Attachment

Estimated changes in OASDI and HI income and outgo resulting from a proposal to eliminate the retirement earnings test at normal retirement age in 1990, fiscal years 1990-99

(In billions)

	Fiscal year										Totals	
	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	1990-94	1990-99
Increase in OASDI benefit payments under a proposal to eliminate the earnings test at normal retirement age after 1989 1/	$3.5	$5.3	$5.4	$5.5	$5.6	$5.7	$5.8	$5.8	$5.7	$5.7	$25.3	$54.0
Net reduction in OASDI administrative expenses 2/	(3/)	(3/)	.1	.1	.1	.1	.1	.1	.1	.1	.2	.6
Increase in OASDI revenues as a result of the Federal income taxation of OASDI benefit payments 4/	.2	.4	.4	.4	.4	.4	.4	.4	.4	.4	1.8	3.8
Net total increase in OASDI cost (prior to the effects of any net increase in work effort induced by the elimination of the retirement earnings test 5/	3.3	4.9	4.9	5.0	5.1	5.2	5.3	5.3	5.2	5.2	23.3	49.6
Estimated offsets to above cost due to increased work effort resulting from the elimination of the retirement earnings test: 6/												
Increase in OASDHI payroll taxes	.1	.2	.1	.1	.1	.1	.1	.1	.1	.1	.6	1.3
Reduction in HI benefit payments due to primary payment by private health insurance 7/	(8/)	(8/)	(8/)	(8/)	(8/)	(8/)	(8/)	(8/)	(8/)	(8/)	.1	.3
Total of offsets	.1	.2	.1	.1	.1	.2	.2	.2	.2	.2	.8	1.6
et total increase in OASDHI cost after estimated effects of induced work effort 9/	3.1	4.8	4.8	4.8	5.0	5.1	5.2	5.2	5.1	5.1	22.5	48.1

/ After 1988, the retirement test would cease to apply beginning with the month during which the beneficiary has attained age equal to the applicable normal retirement age.

/ Estimates based on information provided by the Office of Budget.

/ Net change in administrative expenses of less than $50 million.

/ Estimates based on information provided by the Office of Tax Analysis, Department of the Treasury.

/ Represents increase in OASDI benefit payments, less (i) net reduction in OASDI administrative expenses and (ii) increase in receipts from the taxation of benefits.

/ The magnitude of this effect is highly uncertain. Investigations of available data on this subject have produced conflicting evidence as to the nature of this induced effect. The estimates shown in the second half of this table represent the evaluation of the Office of the Actuary based on (1) data collected from the Social Security Administration's Continuous Work History Sample, and (2) independent studies of this issue. Actual amounts could be substantially different.

/ Estimates based on information provided by the Office of the Actuary, Health Care Financing Administration.

/ Reduction in benefits of less than $50 million.

/ Represents net increase in OASDI cost shown in top half of table, less offsets due to induced work effort shown in bottom half of table. See footnote 6 concerning the reliability of effects of induced work effort.

otes: 1. Totals may not equal sum of components due to rounding.
2. All estimates are based on the alternative II-B economic and demographic assumptions from the 1989 Trustees Report.

Social Security Administration
Office of the Actuary
June 22, 1989

In 1972, the retirement test was liberalized when the dollar-for-dollar withholding rate was changed to a rate of $1 of benefits withheld for every $2 of earnings over the exempt amount. In 1977, the test was substantially liberalized when the exempt amount was increased by $1,000 in 1978 and by increments of $500 in each of the next 4 years. What was the response of the labor force to these liberalizations? How does the value in real dollars of these increases in the exempt amount compare with the value in real dollars of some of the most recent proposals to raise the exempt amount--namely, increasing the threshold by $1,040 in 1990, or increasing it in $3,000 increments for 3 years?

Past studies of retirement earnings test liberalizations have generally not identified any clear labor force response to the changes.

The chart below shows the current dollar value (in 1989 dollars) of prior year increases in the annual exempt amount for 1973-83.

Year	Annual Limit	Actual $ Increase	Value of Increase in 1989 $
1973	2,100	420	1,157
1974	2,400	300	744
1975	2,520	120	273
1976	2,760	240	516
1977	3,000	240	484
1978	4,000	1,000	1,876
1979	4,500	500	842
1980	5,000	500	742
1981	5,500	500	673
1982	6,000	500	634
1983	6,600	600	737

Chairman **Jacobs**. That last remark of mine means you get to go now. Thank you very much.

Mr. **Enoff**. I appreciate it. Thank you.

Chairman **Jacobs**. Our next witness is Dr. Nancy Gordon from the Congressional Budget Office, sometimes called the CBO. That sounds strangely like CEO.

STATEMENT OF NANCY GORDON, ASSISTANT DIRECTOR, HUMAN RESOURCES AND COMMUNITY DEVELOPMENT DIVISION, CONGRESSIONAL BUDGET OFFICE

Ms. **Gordon**. It is a pleasure to be here, Mr. Chairman, Mr. Brown. Last fall, we testified on the Social Security earnings test before the subcommittee based on a staff working paper we had prepared at your request.

This week, we prepared a memorandum that is in your packet that addresses one particular aspect of the debate over the earnings test. That issue has to do with the economic well-being of people who have earnings that are above the earnings test limit.

[The memorandum appears at the end of this statement.]

Ms. **Gordon**. In looking at economic well-being, we considered a person's family income and divided that family income by the appropriate poverty threshold. For example, for an elderly individual, we took that elderly individual's income and divided say, in 1989—by roughly $5,900, which is the poverty threshold this year.

We did that to adjust for the fact that people live in different size families and a married couple needs more income to have the same standard of living than an individual would. So if this hypothetical individual, for example, had an income of about $12,000, then his or her income-to-poverty ratio would be about two.

The table on the last two pages of the memorandum shows different groups of people in the various columns.

I should also mention here this table is based on data from 1987.

If you go down the rows in the table, you see people who have different levels of income relative to poverty. The first row, then, shows people with incomes relative to poverty that are less than one. In other words, that is the elderly group that is actually poor.

The first column refers to the entire elderly population. The first number in that column, 12.2, that tells you that 12.2 percent of the elderly population is poor. If you go to the fifth row of that column, you will see the figure 24.5, which tells you that about 25 percent of the elderly have incomes that are at least four times the poverty threshold.

The next four columns of this table deal with people who are ages 65 to 69. The last of those four columns indicates the people who had earnings above the exempt amount.

Thus, in so looking at the first number of the column that is labeled "Earnings Over $8,160," you can see that virtually none of the people who had earnings over the limit was poor, whereas if you consider the other groups of the elderly, such as those who are over age 69, you can see that their poverty rates are all considerably higher. For example, for those ages 70 to 74, you have a 10.8 poverty rate. Moving over to the column at the far right those who are age 85 and over—you have a poverty rate of 19.2 percent.

The bottom line is that, among elderly people, those who are 65 to 69 are generally better off than those who are over 70. Furthermore, among people—ages 65 through 69, those with earnings are better off than those without. Not surprisingly, having earnings over the exempt limit makes one even better off.

The other main finding from this table is shown by comparing the middle panel and the bottom panel. The middle panel looks at elderly people who are living with their spouses, mostly married couples, while the bottom panel concerns single women.

If, for example, you look at the category for age 85 and over in the far right hand column, you see that married people have a poverty rate of only 8.8 percent, whereas if you drop down to the third panel which shows unmarried, elderly women you find that they have a poverty rate of over 23 percent. In other words, regardless of age, being part of a married couple makes you better off than if you have become widowed or widowered.

[The memorandum referred to follows:]

CONGRESSIONAL BUDGET OFFICE
U.S. CONGRESS
WASHINGTON, D.C. 20515

Robert D. Reischauer
Director

MEMORANDUM

May 23, 1989

TO: Sandy Wise

FROM: Ralph Smith
Bob Williams

SUBJECT: **The Incomes of Workers Affected by the Earnings Test Compared with the Incomes of Other Elderly Groups**

The table attached to this memorandum uses data from the most recent Current Population Survey to compare the 1987 incomes of workers ages 65 to 69 who are affected by the Social Security earnings test with those of other elderly groups. The results for workers ages 65-69 are similar to those reported for 1986 in "The Social Security Earnings Test and Options for Change," a Congressional Budget Office staff working paper prepared for your Subcommittee in September 1988. Our findings are also subject to the same limitations detailed in that paper. As you requested, the current analysis goes beyond the earlier one by comparing the incomes of workers ages 65 to 69 with the incomes of people age 70 or older.

This memorandum does not address other issues relevant to the debate over proposals to relax or eliminate the Social Security earnings test. For example, we do not address issues concerning the marginal tax rate on earnings faced by some elderly people as a result of the earnings test, the effects of the test on the supply of labor, the administrative complexity of the test, or the budgetary effects of the proposals.

Methods, Data, and Limitations of the Analysis

This analysis is based on data from the March 1988 Current Population Survey (CPS), which contains information about the incomes received during calendar year 1987 for a nationally representative sample of the noninstitutionalized population.1/

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1. The focus of this analysis is people, rather than family units. These findings, therefore, differ from those reported in Committee on Ways and Means, The Economic Status of the Elderly, WMCP: 101-7, 100:1 (May 23, 1989), prepared by the Congressional Budget Office at the request of the Subcommittee on Social Security. In that Committee Print, the units examined were the elderly who lived alone or only with their spouses. (Married couples were included if either spouse was at least age 65.) For this memorandum, all people age 65 or over, not living in institutions such as nursing homes, were included.

For this analysis, we disaggregated the elderly population by age, marital status, and, for the age 65-69 group, by their own earnings. (Earnings included wages, salaries, and self-employment income.) In 1987, the earnings limit for Social Security recipients ages 65-69 subject to the annual earnings test was $8,160. We used this amount to categorize the workers in this age group.

Our measure of economic well-being is the total cash income of a person's family in 1987 expressed as a percentage of the poverty threshold applicable for that family. Poverty thresholds are designed to reflect the differential needs of families of various sizes, so expressing income relative to the appropriate poverty threshold may be a better measure of well-being than income alone. For example, for an elderly person living alone, family income was divided by $5,447; for an elderly couple with no other family members living in the same household, the couple's income was divided by $6,872; and for a three-person family, income was divided by $9,056. (The corresponding poverty thresholds in 1989 are estimated to be about $5,900, $7,500, and $9,900, respectively.)

Because of time and data limitations, the only variables used to depict whether individuals might have had their Social Security benefits reduced by the earnings test were their age and their annual earnings. We did not exclude the elderly who recently retired and therefore would have been subject to a monthly earnings test or those who were otherwise not eligible for Social Security benefits. Likewise, we did not estimate the amount by which their Social Security benefits were reduced or the extent to which the benefits of workers' dependents were affected. Another limitation of this analysis is that we did not take into account any behavioral responses that might have resulted from the operation of the earnings test.

Findings

Table 1 summarizes our results. The first column shows that 12.2 percent of the 28.5 million elderly were poor in 1987 – that is, were in families in which the total cash income was less than the applicable poverty threshold, making the ratio less than 1.0. At the other extreme, almost 25 percent of all elderly were in families with incomes at least four times their poverty threshold (over $21,788 for an elderly individual and $27,488 for an elderly couple living alone in 1987).

The next four columns focus on the 9.8 million people ages 65 through 69. Three-quarters of this group (7.3 million people) did not work during 1987, and another 15 percent had earnings below $8,160; just 11 percent had earnings high enough to be subject to the earnings test. Whether or not they were earners, the 65-69 age group was better off than the entire elderly population. Furthermore, within the group, those with earnings--and especially those with earnings over $8,160--were the best off. For example, while 11 percent of people ages 65-69 with no earnings were poor in 1987, only 5 percent of those with earnings less than $8,160, and virtually no one with earnings above the exempt amount, were in poverty.

The remainder of the table shows that family incomes of older cohorts tend to be lower than those of younger ones and that they are highest among married couples and lowest among unmarried women. For example, the poverty rate rises from 9.0 percent of the population ages 65-69 to 19.2 percent of the population age 85 and over. Likewise, the percentage with incomes at least four times the poverty threshold is lowest for the oldest group -- 15.8 percent -- compared with 29.8 percent for those ages 65 to 69. At each age, married couples have much higher incomes than single women. Moreover, in the upper age groups, single women account for a much larger share of the population -- 1.4 million single women age 85 or older compared with 530,000 married people living with their spouses and about 370,000 single men that old. Consequently, the low incomes of unmarried elderly women contribute to the substantial poverty of the oldest group.

TABLE 1. DISTRIBUTION IN 1987 OF PEOPLE AGES 65 AND OVER, BY MARITAL STATUS, FAMILY INCOME RELATIVE TO POVERTY THRESHOLD, AND EARNINGS (In percent)

Family Income Relative to Poverty Threshold	Total, Ages 65 and Over	Ages 65 through 69				Ages 70-74	Ages 75-79	Ages 80-84	Ages 85 and Over
		Total	No Earnings	Earnings Up to $8,160	Earnings Over $8,160				
				All Elderly People					
Under 1.0	12.2	9.0	11.0	5.2	0.1	10.8	14.5	16.9	19.2
1.0-1.99	28.4	23.0	25.8	23.7	3.1	27.1	32.9	33.7	37.3
2.0-2.99	21.2	21.5	22.1	26.7	10.3	22.8	20.9	19.6	17.0
3.0-3.99	13.8	16.7	16.6	16.2	18.6	14.2	11.3	10.3	10.8
4.0 and Over	24.5	29.8	24.4	28.2	67.9	25.2	20.5	19.4	15.8
All	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Number in Group (in thousands)	28,527	9,805	7,284	1,429	1,091	7,667	5,540	3,219	2,296
				Elderly People Living With Their Spouses					
Under 1.0	5.9	4.7	5.8	2.7	0.1	5.2	7.2	11.0	8.8
1.0-1.99	23.0	18.7	21.7	17.3	2.8	22.1	28.9	30.7	38.2
2.0-2.99	23.8	22.0	23.3	25.8	9.4	25.1	25.1	24.6	27.1
3.0-3.99	16.8	19.2	19.8	17.8	17.0	17.8	13.3	11.0	9.3
4.0 and Over	30.5	35.4	29.4	36.3	70.7	29.8	25.6	22.8	16.6
All	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Number in Group (in thousands)	15,573	6,634	4,883	949	802	4,543	2,724	1,143	530
				Other Elderly Women					
Under 1.0	21.0	19.5	23.3	10.7	0.0	20.1	21.6	21.6	23.3
1.0-1.99	35.6	32.5	34.8	35.9	5.4	36.0	37.3	36.6	35.9
2.0-2.99	17.5	19.7	18.7	28.6	13.8	18.5	16.3	17.5	14.1
3.0-3.99	10.1	12.1	10.4	13.2	25.9	8.8	9.7	9.1	11.1
4.0 and Over	15.8	16.1	12.7	11.6	54.9	16.6	15.1	15.2	15.7
All	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Number in Group (in thousands)	10,008	2,308	1,779	336	193	2,403	2,237	1,664	1,396

(continued)

TABLE 1. (Continued)

Family Income Relative to Poverty Threshold	Total, Ages 65 and Over	Ages 65 through 69				Ages 70-74	Ages 75-79	Ages 80-84	Ages 85 and Over
		Total	No Earnings	Earnings Up to $8,160	Earnings Over $8,160				
				Other Elderly Men					
Under 1.0	16.1	13.9	17.2	8.8	0.0	14.7	21.1	14.6	18.2
1.0-1.99	32.2	30.0	32.7	37.4	0.9	28.7	35.1	30.6	41.5
2.0-2.99	19.6	22.3	22.8	27.9	10.6	22.6	18.8	14.6	13.9
3.0-3.99	10.2	10.4	8.7	12.9	17.5	9.6	8.1	13.0	11.6
4.0 and Over	21.9	23.5	18.6	13.0	71.0	24.5	16.9	27.2	14.9
All	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Number in Group (in thousands)	2,946	863	623	144	96	722	579	412	371

SOURCE: Congressional Budget Office tabulations of data from the March 1988 Current Population Survey.

NOTES: Details may not add to totals because of rounding. In this table, the ages 65-69 group includes some people who were not subject to the annual earnings test because they retired during the year.

Chairman **Jacobs**. That is, if you get along.

Ms. **Gordon**. If you get along, or if it is worth it to have a higher standard of living.

Chairman **Jacobs**. Mr. Brown.

Mr. **Brown**. Seeing that the chairman has just recently responded to the incentive in the Social Security law that rewards marriage, we probably have made our case for incentives very well this morning.

Chairman **Jacobs**. No doubt about it. All cottage cheese is made in cottages.

Mr. **Brown**. What this table seems to suggest is that of all elderly poor, of those from 65 to 69 who have some earnings, 5.2 percent of them are living below the poverty level.

Ms. **Gordon**. That is right—5.2 percent of the people in this age group with earnings up to $8,160 in 1987 were poor.

Mr. **Brown**. And you have 23.7 percent living at the poverty level, or up to 1.999?

Ms. **Gordon**. Yes, up to twice the poverty level.

Mr. **Brown**. Thus, if the supposition is that the penalty or test, as some have called it, restricts earnings beyond that level, those would be the groups that would primarily be affected, then, I take it, at least in terms of moving out of the poverty level or the area close to it.

Ms. **Gordon**. Very few elderly people who have earnings above the limit remain poor. With earnings at exactly that level, no Social Security benefits, and no other income, you have to have at least three people in your family in order to be poor.

If you had earings just at the limit, and you also had some Social Security benefits to add to those earnings, your family would have to be even larger for you to be poor, and very few elderly live in such large families. In other words, because their families are large, they still remain poor even though their incomes in dollar terms are reasonable, the earnings limit plus their Social Security benefit.

If you have enough earnings to eliminate your benefit completely, your earnings have gone up so much that you are moving down this column. You are moving higher and higher above the poverty threshold.

Mr. **Brown**. Help me with our calculations. I know in calculating the poverty rate, we do not count certain noncash benefits.

Ms. **Gordon**. That is true.

Mr. **Brown**. Which benefits fall into the category that would affect the elderly? For example, does Medicaid and nursing home coverage—does that count?

Ms. **Gordon**. None of the noncash benefits is considered when we calculate poverty rates. It is just cash income. Therefore, things like food stamps, subsidized housing, Medicaid, or Medicare—the latter being by far the biggest of the noncash benefit programs for the elderly—are not counted, even though they are of substantial value to some of the elderly.

Mr. **Brown**. How would that change your table that shows the poverty level starting a little over 10 percent at age 70 to 74, going up to 19.2 percent of age 85 and over?

If you counted those benefits, how that would change the portion living in poverty?

Ms. **Gordon**. We have done a fair amount of work on examining some of the noncash benefits. Generally, what we find is that the actual numbers decline a little bit, but the patterns remain the same. So you would still find that those who were ages 70 to 74 were much less likely to be poor than those who were age 85 and over.

Mr. **Brown**. I see.

Ms. **Gordon**. Thus, the story would not change very much, but the actual numbers that you would see on the table would all go down if you included those noncash benefits.

Mr. **Brown**. Well, I am thinking in terms of those folks who are in nursing homes in which Medicaid pays the full cost.

Ms. **Gordon**. They are not included in this table, since it is based on the current population survey, which does not include institutionalized people. Someone who is living in a nursing home, therefore, would not be reflected in the table at all.

Mr. **Brown**. So institutionalized people—I take it can be for any area—don't come under these figures at all?

Ms. **Gordon**. That is right.

Mr. **Brown**. That could include people in prisons, as well as people in nursing homes?

Ms. **Gordon**. That is right.

Chairman **Jacobs**. And Congress.

Mr. **Brown**. The chairman adds Congress. I have never thought of us as poor, Mr. Chairman.

Ms. **Gordon**. Congressmen and Congresswomen are included in the table.

Mr. **Brown**. Only those Members of Congress who refuse to accept their pay raise might fit into the poverty category.

Chairman **Jacobs**. Marriage is an institution, too. You had better clarify that.

Mr. **Brown**. I fear I am on very dangerous ground and will pass further questions.

Thank you.

Chairman **Jacobs**. Thank you, Dr. Gordon. We appreciate your contribution to the record.

Ms. **Gordon**. Thank you.

Chairman **Jacobs**. And our next witness is our friend, Hon. Arthur S. Flemming, former Secretary of the Department of Health, Education, and Welfare, and we are going to have to start adding, since we discovered it, a former member of the National Security Council, and present great guy.

STATEMENT OF HON. ARTHUR S. FLEMMING, FORMER SECRETARY, DEPARTMENT OF HEALTH, EDUCATION, AND WELFARE

Mr. **Flemming**. Thank you, Mr. Chairman. I appreciate the opportunity of participating in this hearing on liberalizing the Social Security retirement test and repealing certain Social Security benefits in order to partially offset the costs of liberalization.

First of all, I would like to suggest that these are the types of issues that should be considered by the next Social Security Advisory Committee in connection with other recommendations that have been or will be made for changes in our total Social Security System.

We know that the system is in close actuarial balance. We know, therefore, that any changes in benefits will have to be accompanied by increases in revenues. But the merits of any proposed changes in benefits should be considered at the same time that the merits of other proposed changes in benefits are considered, and choices should then be made in the light of specific recommendations for increases in revenues.

This is a task that historically has been undertaken by Social Security advisory bodies, and these recommendations have been found to be helpful by both the executive branch and the Congress.

The process involved in the Social Security advisory body approach helps us to avoid the temptations of a patchwork approach. The next Social Security Advisory Council is scheduled to be convened shortly.

I recognize that the retirement test was made a part of the Social Security System at the outset in order to answer the question, when has a person retired and is therefore eligible to begin drawing benefits.

In the early days of the system, it was a stringent test. Beginning in the 1950's, a policy was put into effect of gradually liberalizing the test. This policy of liberalization continues.

For example, beginning in 1990, benefits will be reduced by $1 for every $3, instead of $2, in excess of the earnings ceiling for persons who reach full retirement age.

In this connection, we should also keep in mind that the delayed retirement credit, which is now 3 percent a year, beginning in 1990 will increase gradually each year until it reaches 8 percent in 2009 and thereafter.

I recognize that reasonable persons can differ on the impact that the earnings test has on older persons responding to opportunities for continued involvement in the work force. Nevertheless, at this point I believe that we must keep in mind that we are dealing with an insurance program and not a pension program.

This means that we must be able to apply some test to determine when people have retired and are entitled to benefits. If we accelerate the liberalization of our present test, we are going to have to spend more for benefits than we are now spending. This means that we must increase our revenues or disturb the close actuarial balance of the system.

I do not believe either policy is a wise policy to follow at this time. Furthermore, I do not believe it would be wise to attempt to cover a portion of the increased costs by a reduction of benefits. Our beneficiaries, no matter how small a number may be involved, should know that they are a part of a social insurance system that does not cut benefits. They should be in a position where they can depend, as a minimum, on continuing to receive the benefits they are now receiving.

I again suggest, Mr. Chairman, that this item be placed on the agenda for the Social Security advisory group that is now being established. Then its merits and demerits can be considered alongside the merits and demerits of other proposals for change.

Chairman **Jacobs**. Dr. Flemming, thank you.

Mr. Brown.

Mr. **Brown**. Mr. Secretary, we appreciate your contribution, as always.

Mr. **Flemming**. Thank you.

Mr. **Brown**. Let me ask, do you see any difference in the merits of liberalizing this test between those that are over 65 versus those that are under 65?

Mr. **Flemming**. No; I would not personally draw the line there. The law does give people the opportunity of applying for benefits at age 62. They are reduced benefits, as we all know, if they apply at 62. And it seems to me that if the test is going to be liberalized that they should have the opportunity of enjoying whatever benefits may flow from that liberalization just as much as the persons who may receive full benefits at 65.

I appreciate the fact that that is one way of adjusting the costs. I have listened to the dialog on that, but I think I would find it a little bit difficult to justify drawing that line if I were confronted with questions from people who fall into the 62 to 65 group.

Mr. **Brown**. The reason I bring it up is because it appears to me that perhaps folks who are under 65 may have a greater ability to work than those above 65, and thus offset the impact.

Mr. **Flemming**. These days, I think it is a little bit difficult to generalize along those lines because I think persons 65 and above—a good many of them are in a position where if they want to continue to be employed full time or part time, they are able to do it.

Mr. **Brown**. Well, your own enormous contribution to our country is good testimony to that. Are you above 65?

Mr. **Flemming**. Yes; I am slightly above 65.

Mr. **Brown**. Thank you.

Chairman **Jacobs**. Dr. Flemming, we appreciate your testimony.

Dick, did you have any questions?

Mr. **Schulze**. No; other than to thank the witness for a cogent presentation.

Mr. **Flemming**. Thank you, sir.

Chairman **Jacobs**. You are the last witness who can get off in time for the traditional lunch hour or, as my father says, dinner hour, Dr. Flemming. We thank you for your testimony.

Mr. **Flemming**. Thank you.

Chairman **Jacobs**. Robert Ball, former Commissioner of Social Security, is our next witness.

STATEMENT OF HON. ROBERT M. BALL, FORMER COMMISSIONER OF SOCIAL SECURITY

Mr. **Ball**. Mr. Chairman, I have been listening to the previous witnesses and trying to identify what I could say that hadn't already been covered, and I, to my surprise, do find a couple of points that have not been addressed.

The first is that whatever you do—whether you decide to continue present law, which, in the long run, results in a long-run cost approximately equal to abolishing the test, or whether you decide to not have a retirement test at all between the ages of 65 and 70—

I would hope that you would not end up by drifting into a situation where people have to choose between the two possibilities.

If individuals are ultimately put in a position where they have to decide whether to take full benefits at 65 and work at the same time, or ask Social Security to withhold their benefits and then get higher benefits when they do retire, lots and lots of people are going to make choices which turn out later to be wrong.

They are going to ask Social Security interviewers what to do, and they will try not to tell them, but it will be difficult not to lead the beneficiary to a decision, and the choice will be one that will not turn out well for many people. To illustrate: you may decide to not take your benefits at the same time you are working—which seems like a very rational choice since you have an income from wages and it makes since to have higher benefits later when you no longer have wages. But supposing at age 70 when you start to get this higher benefit, you find you have a fatal disease and you are going to live only a year or less. Well, you and your family would have been better off to take the lower benefits earlier.

Or take the reverse situation: Supposing you decide that instead of postponing, you will take your benefit immediately and have it at the same time you have your earnings, then when you do retire at 70, and no longer have any wages, you find you have a much lower benefit than a lot of your friends who postponed taking the benefits. You find, in fact, that you are quite pinched financially. You might even join an organization to petition the Congress to change the law to increase your benefit.

Choices are OK but not when there is no way people can know what the right choice is. So I am urging you not to, by a series of ad hoc liberalizations drift into a situation where you end up with people having to make those choices. In big benefit programs like Social Security it is usually much better that major benefit decisions flow automatically from the law and people don't have to guess what the future holds.

I agree with a lot of things that have been said on both sides of the argument, and I don't want to repeat them, but another point that has not been emphasized is that all liberalizations in Social Security should be fully financed, even relatively small increases in costs.

There is no extra money in Social Security.

The last report of the trustees showed the system to be slightly out of what we have traditionally used as a measure of close actuarial balance. There is, over the whole 75 years, a seven-tenths of 1 percent deficit, that is 0.02 percentage point out of the traditional measure of close actuarial balance, defined as a deficit under 5 percent of the cost of the program.

Now, I agree with the trustees that this small deficit is not a problem that needs to be addressed currently. Over 75 years, there is enough possibility of being wrong on this so that immediate action on such a small deficit isn't needed, particularly since the 50-year estimate shows a plus of 0.44 percent of payroll.

But at the same time, I don't think it is wise to add to either the long-range deficit or to short run cost without full financing. In the short run, abolishing the test, as compared with present law—

which has an 8-percent increment coming along later—does have significant cost.

The proposals that have been made for a series of $3,000 increases in the exempt amount and then abolition have been structured so there is only a $6 billion cost over the next 5 years in order to minimize costs for Gramm-Rudman purposes. But from then on, for many, many years in the future, the cost is about $5 billion a year.

The third point that seemed to me wasn't stressed very much by previous witnesses is that if you do abolish the test you have at the very least a public relations problem. The spectacle of high-paid executives getting Social Security benefits at the same time that they continue to earn large salaries will add weight to the case that some people make in favor of an income test or a means test in Social Security. If there were such a test added to the program, it would ruin Social Security; it would absolutely destroy it. So this perception problem of people continuing to work, having large incomes and also getting Social Security, can become a serious threat if the test is abolished.

But I have to say it is also something of a problem in present law if these same executives get a much bigger benefit after they retire than is presently the case. This is not a simple matter. You may want to consider not just the changes before you but these changes in relation to the policy on the taxation of Social Security benefits.

I would argue that if you are going to buy benefits at the same time people work at good salaries or even pay larger benefits later to high-paid people as under present law that you probably would want to at the same time, to tax more of their Social Security benefits.

The perception of unfairness from people getting those benefits and not paying a full income tax on that part of their benefit that exceeds what they themselves have contributed, I think, would be too bad. So I think you should consider not just these changes, but the relationship of retirement test changes to the taxation of benefits. That makes these proposals more complicated than they appear to be at first.

Finally, Mr. Chairman, the specific way in which at least one of the proposals suggests financing the plan—dropping certain retroactive provisions—ought to be examined on its own merits. Should those retroactive provisions be dropped or not?

There should be a burden of proof on people who want to drop benefits—about 100,000 people are affected. My own view is that, you could justify modification of the present provision by dropping part of it, but that, on the other hand, there is a pretty good case for another part of the retroactive provision that would also be dropped by the proposal before you.

But my main point isn't that. I am not here to defend these particular retroactive provisions. But if you are going to save that money, I think you have to face the question, is this the best way to spend it? I believe the CBO table is very impressive in terms of who benefits from changes in the retirement test, as compared to various other things that could be done. If you decide that you want to cut back anywhere in Social Security, where do you want to spend the additional money?

I would end by endorsing Secretary Flemming's suggestion that there is enough involved in the various proposals before you on the retirement test—their interrelation to the taxation of benefits, the question of what other things might be done with any savings—that you might benefit from directing that the next Advisory Council on Social Security consider this matter and report back to you.

Obviously, you don't have to pay any attention to them if you don't like what they say, but they will have a couple of years to consider Social Security clauses in relation to other matters. Over the years has been that the council's recommendations have proven largely to be quite useful.

Thank you, Mr. Chairman.

[The statement of Mr. Ball follows:]

TESTIMONY OF ROBERT M. BALL

My name is Robert Ball. I was Commissioner of Social Security from 1962 to 1973. Prior to my appointment by President Kennedy I was a civil service employee of the Social Security Administration for some twenty years. Since leaving the government in 1973, I have continued to write and speak about Social Security and related programs. I was a member of the 1978-79 Advisory Council on Social Security and more recently was a member of the National Commission on Social Security Reform, the Greenspan Commission, whose recommendations were included in the 1983 Amendments. I am testifying today as an individual and the views expressed are not necessarily those of any organization with which I am associated.

As I understand it, this hearing has been called to consider two proposals for further liberalizing the earnings or "retirement" test as it applies to Social Security beneficiaries between "normal retirement age"[1] and the attainment of age 70:

(1) A proposal to increase the exempt amount in 1990 by about $1,000 more than the automatic increase that will take place anyway; and

(2) A proposal to increase the exempt amount by $3,000 above the automatic increase in 1990 by another $3,000 in 1991, an additional $3,000 in 1992, and complete elimination of this test by 1995. You also have asked for views on the repeal of certain retroactive Social Security benefits as a way of partly paying for a retirement test liberalization.

Mr. Chairman, it seems to me that before acting on any of these proposals, the Committee may wish to consider the relationship of the proposals to several provisions already in present law but slated to become effective later and the relationship of the proposals to the Committee's long-run policy on the retirement test. And then, too, the questions arise whether the cuts in retroactive benefits are desirable and, if so, whether the savings from cutting such benefits are best used for this particular purpose.

Provisions in Present Law Not Yet Effective

As a result of the 1977 and 1983 amendments, several provisions of present law will reduce the impact of the retirement test in later years. In 1990 the reduction of $1 for each $2 earned above the exempt amount by those 65 and over will become a reduction of $1 for each $3 earned, allowing all those over 65 and affected by the retirement test to keep more of their benefits. This change addresses one of the major objections to the retirement test, the high marginal rate of reduction faced by beneficiaries who earn above the exempt amount. Under present law, this marginal rate reduction will drop in 1990 from 50% to 33.3%. This change increases incentives to work much more than merely shifting upwards by, say $1,000, the band of earnings to which the marginal rate applies. The great majority of beneficiaries earning above the exempt amount would not see a change in the utility of earning more because of raising the exempt amounts unless the increase is very large, but all will be affected by the change in the marginal rate of reduction.

Further, under present law, the totally exempt amount in the retirement test rises automatically every year as wages rise. Since wages ordinarily rise more than the cost of living, the present provision provides year by year for an increased living standard on the part of working beneficiaries affected by the level of the exempt amount. This yearly liberalization of the test continues indefinitely.

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[1] "Normal retirement age" is now 65 and rises gradually to 67 beginning with those attaining age 62 in 2000 having a normal retirement age of 65 and 2 months and reaching 67 for those attaining age 62 in 2022 and later.

Perhaps most important, present law provides that for those who became 62 in 1987 and 1988, the addition to their benefits on retirement for each year of work from age 65 to age 70 will rise from the present bonus of 3% a year to 3 1/2% and for those who attain age 62 this year and next, the bonus will be 4%. The increment continues to increase every two years until for those attaining age 62 in 2005 and later, the benefit increase will be 8% for every year worked after normal retirement age and before age 70. On average, the 8% a year increase is approximately the equivalent of taking benefits at normal retirement age and receiving them over a longer life expectancy as compared to taking the higher benefit later over a shorter life expectancy. In other words, under present law from 2005 on, those who work after the normal retirement age will get the actuarial equivalent of the benefits foregone by working; in the long run the cost to the Social Security program of paying higher benefits to those who work will be approximately the same as if the retirement test were abolished and benefits were paid at normal retirement age whether or not employment continues.

The main difference between present law and proposals to abolish the retirement test are that under present law people will not receive their benefits at the same time they work at relatively high wages but will receive larger benefits later when they have retired. If the test is abolished they will be able to get both wages and a Social Security benefit at the same time, but if they make that choice, the benefit will be substantially lower during their retirement years.

Another difference is that present law gradually moves to an increment for work which is the actuarial equivalent of abolishing the retirement test, but the full equivalent is not reached until 2005. The cost of this gradual change is already included in the financing of the program. Proposals to abolish the test before 2005, say by 1995, therefore, have a cost that has not been taken into account in the financing of the program.[2] The proposal to raise the exempt amount in $3,000 steps beginning next year and abolishing it in 1995 is estimated to cost somewhat over $6 billion during the next five fiscal years as compared to present law and about $5 billion a year for many years thereafter. The long-range cost of abolishing the test over the 75 years for which the estimates are usually made is estimated to be only 0.01% of payroll but there is a significant cost over the next 20 years or so. (The Social Security actuaries have increasingly taken into account in their estimates the fact that fewer and fewer people are working past age 65 and thus have given lower and lower cost estimates for retirement test liberalizations. It is possible that the costs will turn out to be higher than now expected because older workers in the future may work more often than older people do currently since fewer younger workers will be available and employers may seek more older employees.)

Both the short-range and the long-range cost of any proposals to liberalize Social Security need to be met by new funds going to Social Security, not just savings offsetting the cost elsewhere in the budget for Gramm/Rudman/Hollings purposes. There is no extra money in Social Security. In fact the 1989 report of the Board of Trustees of the Old-Age and Survivors Insurance fund shows the system to be slightly out of "close actuarial balance" as traditionally defined--that is a deficit over the 75 years that is less than 5% of the cost of the program. The II-B estimates, the ones usually used for judging the actuarial status of the system, now show a deficit of 0.7% of payroll, 0.02% of payroll outside the definition of close actuarial balance. I agree with the trustees that this slight long-range deficit is not a problem that needs to be addressed now. Seventy-five year estimates have too wide a range of possible error for a -.02% of payroll to be considered a pressing problem and the fifty year estimates show a comfortable surplus (0.44% of payroll) but nevertheless, it would be unwise to add to the estimated deficit. In my view, all proposals for liberalizing Social Security should be fully financed.

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[2] As a matter of fact, these costs continue for some time even after 2005 since workers between the normal retirement age and 70 could get full benefits if the test is abolished, while under present law only those who reach age 62 in 2005 and later get the full actuarial increment.

I am not sure whether it is preferable to continue with present law or ultimately to abolish the test at the normal retirement age. Either approach presents problems and each has some advantages. The spectacle of high earning executives getting Social Security benefits while fully employed after age 65 could add force to the argument of those who want to condition benefits on some sort of income test or means test, a change that I believe would destroy the whole character of the Social Security system, and it is certainly more difficult to argue for a full cost-of-living adjustment for those who are also getting full wages. At the same time, paying these same high earners substantially more after retirement because of the increase in the delayed retirement credit has somewhat the same problem, although probably to a lesser extent. At the very least, in either case, I would think the Committee would want to apply the income tax to the Social Security benefits of high-income recipients to the extent the benefits exceed what these earners have contributed to Social Security. This would mean taxing about 85% of Social Security benefits for such people rather than 50% as at present. Otherwise the ultimate result of either present law or abolishing the test would seem to be unduly favorable to the well-off. It is not as simple as it seems to make changes in the retirement test. There are other policy implications such as the issue of taxing more of the benefit.

On the positive side, either the changes that will take place because of present law or abolishing the test adds to incentives to continue working, which, by and large, I believe is good for the economy and, at least on a part-time basis, good for a high proporion of 65 to 70 year olds. I do not think it is wise, however, to end up with both of these provisions in effect at the same time. The result would be to require people to choose whether they want to take lower benefits at the normal retirement age or wait to they stop working in order to receive the higher actuarial equivalent. One of the more appealing points about abolishing the retirement test is the great simplification that would occur. The elimination of many errors in administration and the avoidance of confusion among beneficiaries would be a very real gain. However if we end up with people having to choose between the two approaches, new complications arise. Social Security employees will be asked their advice and whatever they say the advice will frequently turn out in retrospect to be wrong.

If you ultimately want to abolish the retirement test, then do it and pay a straight annuity at 65. If you want to give people more when they do retire but not pay them while holding good paying jobs, do that, but I hope you will avoid drifting into a situation where people have to try and predict their future. The choices, on average, are actuarial equivalents but in practice for the individual and their families they will in many cases turn out differently than they expected. For example, a decision to postpone benefits until age 70 and get a higher benefit on retirement may look attractive at the time made, but if the beneficiary is taken fatally ill shortly after retirement, it will prove to have been the wrong choice. Or in the reverse, some of those who choose immediate benefits may feel a real pinch after age 70 and envy their contemporaries who have substantially higher benefits. Some may even join an organization to try and get you to raise their benefits! In a huge program like Social Security it is usually better to avoid giving choices on important benefit decisions because there is no way of telling ahead of time what the right decision is.

Basic Policy On the Retirement Test

It does not seem wise to me to make further ad hoc changes in the retirement test until the Committee determines first where it ultimately wants to come out. The history of the test has been one of continual liberalization, pretty much on an ad hoc basis without full attention to the consequences. I am as guilty as anyone, having proposed or gone along willingly with most of the changes.

Perhaps now is the time to step back and take a more fundamental look at the overall policy--perhaps with the help of the soon-to-be-appointed statutory Advisory Council on Social Security.

The original idea of Social Security was to pay benefits only when there had been a loss of earnings due to retirement in old age or the death of a wage earner and later the total and long-term disability of a wage earner. It was not considered an annuity paid automatically at a given age. And contribution rates were set in accordance with the risk of being retired after age 65, not just reaching that age, an approach which saved money. This concept has been preserved in the case of disability--benefits are paid only if a worker is unable to perform substantial gainful activity. But in the case of retirement the concept has been whittled down to the point that it now amounts to very little.

Originally retirement benefits were paid only if earnings were below $15 a month (1939). Gradually this amount was raised. As earnings in general rose, it seemed reasonable enough to consider people retired who earned up to $50 a month (1950) and then $75, $80 and by 1958, $100 a month. And the higher the amount went, the more troublesome it seemed to make the loss of a whole month's benefit depend on earnings just over or under a specified dollar amount--so the concept of an exempt amount and a dollar reduction for each two dollars earned above that amount was born in 1960, turning the test into a test of gradual or partial retirement rather than complete retirement.

And then with coverage of the self-employed (1950) an annual test was required for them since self-employment net income cannot reasonably be computed on a monthly basis. In 1977 the monthly test of retirement was eliminated for wage earners though it was quickly restored for the first year of retirement. (In the first year there is also a monthly test so that benefits can begin when the worker retires regardless of previous earnings in that year.)

Coverage of the self-employed also introduced the idea of paying benefits at a specified date without regard to work--75 at first (1950), later 72 (1954) and 70 (1981). The idea of paying without a retirement test after a specified age came in because one of the arguments of the opponents of covering the self-employed was that lawyers, doctors and other self-employed persons never retired and would get nothing for their contributions, so a change was agreed to that made the program insurance against wage loss up to a certain age and then a straight annuity payable at a given age after that.

And there were several times when liberalization in the retirement test seemed the only alternative to its complete abolition, which would have added to costs and resulted in less money available for the bulk of beneficiaries who were not at work.

As the test has developed, the public has found the provisions difficult to understand. Why and how benefits are withheld is frequently mysterious, and many people apparently limit their annual earnings to the wholly exempt amount, not wanting to risk going off the benefit rolls for awhile, with uncertainty about overpayments and uncertainty about when and if they would start getting benefits again.

Whatever you ultimately decide is the right long-run direction, choosing between (1) the present law actuarial increase for work or (2) no retirement test at all past normal retirement age, I see little argument for making still another of these ad hoc liberalizations, particularly when the financing for the liberalization comes from cutting benefit rights now available and, when the financing available to the Social Security fund, moreover, is not sufficient to cover the cost of even the $1,000 increase beyond the first couple of years. It would seem to me to be preferable to take a basic look at the fundamental policy before acting. You might even decide that there is a case to be made for the old concept of insurance against lost earnings. Why should benefits be paid to full-time workers just because they have reached a certain age? Or why should those who are lucky enough to keep their jobs between normal retirement age and 70 get substantially higher benefits when they do retire? Couldn't the money be spent to better purpose on those who have to stop work? Actuarial equity and work incentives are not the only considerations.

It really is not unfair to operate the program as a retirement system making up for lost wages. It depends on what you want to do. The retirement system approach is the less expensive approach, but the annuity approach has better incentive effects. There is a reasonable case on both sides, but a decision should be made on the long-run objective so as to avoid a step-by-step drift toward an annuity concept through a continuing series of ad hoc liberalizations while also retaining the choice of getting an actuarial equivalent benefit after retirement.

The Financing Proposal

Whether retroactivity of reduced benefits should be cut back in certain cases, it seems to me, ought to be decided on its own merits. If this is a desirable action, then it should be done. If it is not desirable, then the benefits shouldn't be taken away to partly finance a liberalization elsewhere in the program. I have not heard a good case for the cuts. By definition they take away benefits that people are now entitled to and propose giving the proceeds to those affected by the retirement test.

There are two steps to this decision: (1) Should the savings be made and (2) if so, is increasing the exempt amount in the retirement test the best thing to do with the savings?

I do not have strong views on maintaining these particular retroactive provisions but they are of importance to some 100,000 people a year. There is a heavy burden of proof on those who would take these benefits away to show it is desirable to do so. Some of the present protections seem quite reasonable to me. For example, the availability of retroactive benefits for the young spouse and/or child of, say, a 63-year-old unemployed older worker, and for the worker himself, does not seem unwarranted; it seems a reasonable protection for such a family against any delay in the worker's filing for benefits due to, say, ignorance of the law or uncertainty about finding work.

In any event, if such savings are made why spend them in this way? Is raising the exempt amount in the retirement test the highest priority use for such savings? I doubt it.

Conclusion

Mr. Chairman, instead of amending the retirement test now, I would hope that you would ask the statutory Advisory Council to study present law, the proposals before you and other alternatives and to report back with recommendations. I believe the full cost of any changes should be covered in the Social Security fund and that any change should fit into a carefully considered long-run policy on the retirement test, including policy on the taxation of benefits if full-time workers are to be granted benefits.

Thank you very much for the opportunity to express my views.

Chairman JACOBS. Thank you, Mr. Ball.

Mr. Schulze.

Mr. SCHULZE. Thank you, Mr. Chairman. Thank you, Commissioner. You have raised some interesting questions and some food for thought. I can say this, that several years ago I talked to many of my wealthier constituents who were in the position you described, and I was surprised.

I thought they would say, gosh, yes, that is no problem, because these were people of great wealth. And I was surprised at the vehemence of their reaction, and they said, no, by God, I worked hard for that and I deserve every penny of it and I deserve it just as much as anybody.

I was really almost shocked. I thought they would say, well, it is just a small amount to me and it doesn't make any difference. But they were just absolutely vehement that that Social Security money was almost sacrosanct. They worked hard, they saved, they paid it. They worked harder than other people; that is why they were so successful.

I guess there really are not easy answers to these problems. Everybody has an emotional involvement and attachment to Social Security.

Mr. BALL. Mr. Schulze, just so I am absolutely clear on the record as to what I meant in relation to these higher-paid people: I feel very strongly that they should receive Social Security benefits. I think it would be a disaster if we started to discriminate on the basis of income.

But I think it does raise the question of whether you shouldn't tax additional benefits if people are going to get high wages and benefits at the same time.

Mr. SCHULZE. Just theoretically? Would you do it across the board? Would it be income-related?

Mr. BALL. I would personally tax that part of the benefit which exceeds what people themselves have paid, which is the policy that, in broad terms, is followed for other retirement systems.

We are now only taxing 50 percent of the benefit, and it would become roughly 85 percent of the benefit if you follow that policy. The proper policy, I believe, in the long run, is to apply that rule to everyone, but the distributional effects of applying it across the board are not too good. I would be content, therefore, to apply the tax to people who have total incomes above specified amounts, as in present law.

Mr. SCHULZE. Back in the middle 1970's, I had proposed that on each Social Security check, the amount the individual had paid in and the amount they had received would be designated. There was a great deal of opposition to that at that time, but I thought it would be educational so that people would maybe better understand the true nature of Social Security and the relationship of the amount that they paid in to that which they received.

Mr. BALL. Of course, this is not a unique Social Security phenomenon. Very typically, people are getting back more than they paid in to a retirement system, but the rule is tax the excess.

Mr. SCHULZE. Thank you, Mr. Commissioner. Thank you, Mr. Chairman.

Chairman JACOBS. Thank you, Mr. Schulze.

I just have one question, and this is a little repetitious, I am afraid. But if a person were 40 years old and said the same thing Congressman Schulze said his constituents said—I paid for it and I ought to start receiving Social Security benefits—we would say, well, now, wait a minute; the thing you paid for was Social Security benefits if you got to be 62 or 65.

Would that really be much different from someone saying I paid for a benefit that was not guaranteed under the law if you didn't retire? Do you see any difference?

Mr. **BALL**. Not really. What people have been paying for under Social Security has been the risk of retirement in old age and earning less than the defined amounts in the law. Now, it is true that in the 1983 amendments, there was a major change when the increment for work between 65 and 70 is going to be raised gradually to the actuarial rate.

Many of the arguments that used to be made against abolishing the retirement test have been considerably weakened by that change. You now have a situation in which, although there is a cost in the short run, the long-range cost of the difference is about one-hundredth of 1 percent of payroll. This is a small amount in Social Security terms.

But it is certainly true, as several witnesses have suggested and the chairman has suggested, that the concept has been—and the contribution rates have been set on this basis—insurance to make up for income lost because of retirement, disability or death.

Now, if you change that to an annuity and you make it a straight annuity at 65, as we have already made it an annuity at age 70, it is slightly more expensive than present law and considerably more expensive than the old idea of an insurance benefit without any increment you work after 65.

Chairman **JACOBS**. Well, my only point is if you go in and pay for a Ford and then slam your fists on the counter and say I want my Rolls Royce because I paid for it, you might be a little off the mark.

We thank you for your contribution to the record, Mr. Ball.

Our first panel—and we will begin strictly the 5-minute rule with the panels, except for Mr. Myers. Our rule here is that officials, and that includes former officials, may have a little more time.

Mr. **SCHULZE**. We have always been eager to hear what Bob Myers has to say.

Chairman **JACOBS**. Mr. Lehrmann is representing AARP. Villers Advocacy Associates is represented by Ronald Pollack; and Mr. Robert J. Myers, a former Chief Actuary for the Social Security Administration, representing his views and his experience; from the Institute of Research on the Economics of Taxation, Mr. Entin; and, finally, the National Council of Senior Citizens, represented by Lawrence Smedley.

So we begin with Mr. Lehrmann.

STATEMENT OF EUGENE LEHRMANN, VICE CHAIRMAN, BOARD OF DIRECTORS, AMERICAN ASSOCIATION OF RETIRED PERSONS

Mr. **LEHRMANN**. Good afternoon, Mr. Chairman. My name is Eugene Lehrmann and I am vice chairman of the board of directors of the American Association of Retired Persons. I have with me Judy Schub, in case we have some technical questions that need to be addressed, from the AARP office.

The association appreciates this opportunity to present its views on the Social Security earnings limit. We commend the chairman of the committee for scheduling this most timely and important hearing.

AARP believes the liberalization of the earnings limit for persons age 65 through 69 would improve the lives of many older workers. Also, it represents good labor, economic, and social policy for an aging society.

It is time to change the retirement test so that it better reflects our population, our work force, and our economy. Given the increased longevity and the generally improved health of many retirees, the prospect of an aging society and shrinking work force, it is important that we find better ways to tap one of our most valuable economic resources—older persons.

The earnings limit is unfair. It penalizes those who work. It can be a significantly loss of income for moderate, and middle-income older persons—$15,000 to $20,000—many of whom work out of necessity, not of choice. AARP believes that these individuals should not be hurt when they seek to improve their economic well-being through work.

Raising the limit would also mean less frustration and inconvenience for beneficiaries. Our members report that explanations of the earning limit provided by the Social Security Administration are confusing, especially regarding the first year of retirement.

Some beneficiaries incur a substantial penalty, 1 month or more of lost benefits, for failing to file a report of estimated earnings in a timely manner. Others face great anxiety and some financial difficulty when they must repay overpayments.

The retirement test not only restricts some beneficiaries' earnings; it also creates administrative problems for the Social Security Administration. The agency estimates that 60 percent of all overpayments and 40 percent of all underpayments result from the earnings limit. Modifying the limit would make fewer people subject to its calculation, reduce the potential for error, and cut Social Security Administration costs.

Despite the fact that many older persons of modest means need extra income and are willing to work for it, some oppose raising the earnings limit. They argue that a change would be costly to the Social Security trust fund.

While there are some short-term costs, the Social Security actuaries estimate that long-term costs to the trust fund are negligible. Moreover, the short-term costs can be offset.

A second argument against raising the limit is that some higher-income individuals would benefit. Modest increases would make a considerable difference to moderate-income beneficiaries, while only making a minimal difference to higher earners.

With respect to any short-term costs of liberalization, the association has looked at a range of offset options within the Social Security Program. These are described in our written testimony.

AARP is prepared to work with the committee to help design a reasonable offset proposal. AARP strongly believes that raising the limit is both fair and intelligent policy. We urge Congress to move ahead on this issue.

AARP again thanks the chairman and members of their committee for their attention and their willingness to consider this important issue. We would be glad to answer any questions you may have.

Chairman JACOBS. Thank you, Mr. Lehrmann.

[The statement of Mr. Lehrmann follows:]

STATEMENT OF THE AMERICAN ASSOCIATION OF RETIRED PERSONS

The American Association of Retired Persons (AARP) appreciates this opportunity to present its view on the Social Security earnings limit (retirement test). The Association has long supported a change in the earnings limit, and we commend the committee for reexamining the matter. Given the increased longevity and generally improved health of many retirees and the prospect of an aging society and shrinking workforce, it is important that we find ways to better tap one of our most valuable economic resources: older Americans.

I The Earnings Limit in Practice

The retirement test limits the amount of earnings from employment that a Social Security beneficiary can receive without a penalty. Because the test applies to a worker's base benefit, it also affects the benefit amount received by his spouse and other dependents.

In 1989 the retirement test is applied to earnings over $6,480 for beneficiaries age 62 through 64 and to earnings over $8,880 for those age 65 through 69. Benefits for a retired worker under age 70 are payable for all months in a year if annual earnings from all types of employment (whether or not covered by Social Security) are equal to or less than the exempt amount. A special monthly test applies in the "initial year of claim" if it produces a more favorable result than the annual test.

II History of the Earnings Limit

Although the Social Security law has always contained a retirement test, over the years it has been modified to narrow the category of affected persons. For example, the age at which the test was eliminated was reduced to 75, then 72 and is now 70. In addition, it was changed from a simple monthly test to one that measured both monthly and yearly earnings. Since 1972, the law has provided for an automatic, annual updating of the retirement test threshold in accordance with changes in annual wages. As well, in 1960 the penalty for excess earnings above a threshold was altered from a total loss of monthly benefits to a reduction in the benefits. The 1983 Amendments further eased the penalty for excess earnings. Beginning in 1990 beneficiaries age 65 to 69 will have benefits reduced $1 for every $3 of excess earnings, instead of the current $1 reduction in benefits for every $2 earned.

Thus, there is ample precedent for reevaluating the retirement test to better reflect the changes in our population, our workforce, and our economy.

III Effects on Beneficiaries

Most beneficiaries are not in the paid labor force and thus will not be affected by any change in the earnings limit. In 1986 eighty one percent of people 65 through 69 did not report any income from earnings. Another twelve percent had earnings below the limit.

About seven percent of the age 65 through 69 population reported excess earnings. That percentage translates to 600,000 people who had benefits either partially or fully withheld. Still others did not elect to apply for benefits because of the test. It is also likely that some people chose to avoid the test altogether by holding their earnings to the limit. (These people are impossible to count).

Among the 12 percent whose earnings remain below the threshold are many moderate income older persons. They rely upon Social Security benefits as their primary retirement income source. Such individuals often were unable to accumulate adequate savings and have little or no pension income. For those among this group who are capable and have the desire to work above the current earnings limit, the opportunity to improve their economic position through employment is constrained. In the words of one of our affected members who has written us:

> "I am not alone in believing the law restricting the amount earned by Social Security is the most unfair and discriminatory law in our beloved United States. The maximum allowable amount is total earnings,and not take home pay...
> "I am an executive secretary, a widow of one year, and I could not possibly live on the allowable earnings and my meager Social Security benefit. Would the government prefer us to live in subsidized low-cost housing, receive food stamps and/or welfare? I am too proud to do that..."

AARP believes we should not penalize moderate income individuals who try to improve their economic situation through the only means available to them -- work. Moreover, our nation benefits from their work effort.

IV Problems Created by the Earnings Limit

A. Administrative

The retirement test not only restricts some beneficiaries' earnings; it also creates administrative problems for beneficiaries and the Social Security Administration (SSA), the agency responsible for the program. Some of these problems would be moderated by changing the earnings limit.

SSA spends over $200 million a year to monitor income levels. The agency estimates that 60 percent of all overpayments and 45 percent of all underpayments result from the earnings limit. Thus, modifying the limit and making fewer people subject to its calculation would reduce the potential for error and SSA's administrative costs. It would mean less frustration and inconvenience for beneficiaries. Our members report that agency-provided explanations of the earnings limit are confusing, especially regarding the first year of retirement. Such misunderstandings create financial and emotional hardships when overpayments must be recouped, especially from a beneficiary who relies upon Social Security benefits coupled with earnings as essential income sources.

Additionally, some new beneficiaries incur a substantial penalty for failing to file a report of estimated earnings in a timely manner. The loss of at least one month's benefit represents a serious financial loss for these persons.
An underpayment, usually the result of overestimating projected earnings, creates its own financial hardship.

B. Decreased Productivity

The earnings limit poses economic problems for our nation as well. Social Security is intended as a partial replacement of income lost due to retirement, disability or death of the worker. However, the definition of retirement has evolved to accommodate changing work patterns. Many older individuals chose to ease out of the workforce rather than drop out. Also, the definition is being modified because some beneficiaries have no choice -- they need additional income.

Moreover, as our society continues to age and the pool of tomorrow's workers fails to keep pace with the demand for labor, older workers will be needed in the workforce. The Census Bureau estimates that in 1995, there will be five million fewer 18-to-24 year olds than there are today. At the same time, according to the Labor Department, the economy is expected to generate 16 million new jobs; 12 million of which will require some education, technical training and experience beyond high school. In light of this, former Labor Secretary William Brock has warned of the possibility of a major skills shortage in this country before the end of the century. Not only will the economy benefit from retaining more older workers, but studies show that the more active and productive persons over 65 tend to remain healthier both physically and mentally than their more sedentary counterparts.

Faced with these demographic projections, our nation must do everything possible to remove employment barriers, reduce age discrimination, change employer attitudes, and eliminate government-enforced disincentives for older persons to work. Efficient use of mature and experienced men and women can have a positive impact upon the general economy.

The 1983 Social Security Amendments contained some incentives for older Americans to remain in the workforce. The Amendments reduced the earnings limit penalty for workers 65 to 69 from a reduction in benefits of $1 for $2 of excess earnings to $1 for $3 in 1990, and it phased-in an increase in the delayed retirement credit (DRC) from 3 percent to an actuarially fair 8 percent by 2008. However, these changes will not do much to alleviate the impact of the earnings limit for today's retired worker.

V CONCERNS ABOUT CHANGING THE EARNINGS LIMIT

Despite the problems that the earnings limit creates, some people assert that changes should not be made. AARP believes that it is time for Congress to seriously examine the recommendations to change the earnings limit. Thus, it is important to examine the merits of the arguments of the opponents of modification.

A. The Cost Concern

Some oppose any change because it could be costly to the Social Security trust funds over the short term if they are not reimbursed. This is true. However, the Social Security actuaries estimate that the long-term costs to the trust funds of liberalization are negligible because the value of the total benefits paid to an individual does not change over his or her lifetime. This is the case because, under present law, an individual whose post-65 earnings result in a loss of benefits receives a subsequent delayed retirement credit. With a liberalization that same beneficiary will receive those benefits now and lose the subsequent delayed retirement credit. Thus, the trust funds actually pay the individual the same amount of total benefits; it is simply that the payout schedule differs.

Certainly, an absolute projection of the revenue gains from the added work effort is impossible because of the uncertainties regarding the numbers of beneficiaries increasing their work effort and the amount of their increased earnings. However, it is clear that additional federal revenues will be collected. The primary sources for the trust funds are the payroll tax and, in some cases, revenue from the taxation of Social Security benefits for those individuals whose adjusted gross income exceeds $25,000 income for singles and $32,000 for couples. Moreover, if the cost of liberalization is offset by additional revenue from changes in the Social Security program, then the cost argument becomes less relevant.

B. Benefit Distribution Concern

There is no question that the higher the threshold is raised, the greater the number of higher earning beneficiaries who would be exempted. However, modest increases will make a considerable difference to moderate income beneficiaries who work out of necessity, not choice. For example, raising the threshold by a modest $1,080, a provision introduced by Senator Armstrong and adopted by the Senate, would have exempted 85,000 individuals with moderate earnings from the limit. This group includes older people who are working at or near the threshold and deliberately hold their earnings down rather than earn over the threshold.

The Congressional Budget Office (CBO) reports that small increases in the limit would exempt a large fraction of low-income families but still leave most people with higher family incomes affected by the test. For example, they note that if the earnings limit had been raised by $1,200 in 1986 to $9,000, families with annual incomes below $15,000 would not have been subject to benefit reductions. Many of those exempted would have been widows, widowers or people who never married. In contrast, a $1,200 increase would have exempted only 5 percent of those with family incomes above $42,000.

When CBO measured income against the poverty level, they found that the significant effects on low income beneficiaries became more apparent. Doubling the 1986 earnings limit ($15,600) would have exempted virtually all people with incomes below three times the poverty threshold. However, almost two-thirds of those with incomes above four-times the poverty threshold would still face benefit reductions.

Finally, the additional income that a moderate income beneficiary receives from a liberalization represents a greater proportion of his or her total income than it does for beneficiaries with higher incomes.

C. Availability of Jobs Concern

Finally, although rarely argued in an explicit manner, the earnings limit is defended as a means of improving the employment prospects of younger workers. This argument seems to be premised on the belief that the earnings limit opens up positions for younger workers and keeps retired workers from re-entering the labor market to compete for jobs, and perhaps even offering their experience and skilled labor at below market rates. While this concern may have had some validity in the late 1930's and early 1940's, it is no longer relevant today.

VI REVENUE OPTIONS

AARP believes it is time to liberalize the current earnings limit. The Association recognizes that the current budgetary situation as well as the constraints imposed by Gramm-Rudman-Hollings necessitate that the cost of any liberalization be deficit neutral. Similarly, a concern about the potential impact on the trust funds of an unoffset liberalization is understandable.

Some believe that CBO's costs estimates for liberalization are more pessimistic because revenues flowing into the trust funds are not counted in their estimates. If the additional payroll tax revenue and taxation of benefits revenue flowing into the trust funds were included in the cost estimates of liberalization proposals, then the negative impact of any liberalization on the trust funds would be moderated.

The Association has looked at a range of revenue offset options within the Social Security program the committee might wish to explore. While each may have drawbacks, we believe each has sufficient merit to be considered in any deliberations on liberalizing the earnings limit.

- Include Newly Hired State and Local Employees in the Social Security Program

Universal coverage has long been a goal of the Social Security system. Today the program covers about 93 percent of the workforce. State and local employees remain the only significant group of workers that are unable to take advantage of the program's benefits.

Most states provide Social Security coverage for at least some of their employees. Approximately 30 percent of all state and local employees do not participate in the program. Instead, these workers may be covered by pension plans set up by the states and localities that have chosen to remain outside the Social Security system.

While it may be financially advantageous to the jurisdictions that remain outside Social Security, such exclusion poses numerous problems for the affected workers. First, these uncovered workers may be forfeiting the special protections that Social Security provides: superior survivor, dependent, and disability benefits; indexed cost-of-living adjustments; and portability from job to job. Additionally, some low income workers might receive a higher benefit than under their current plan because Social Security has a progressive benefit formula. Some work for many years in noncovered employment and receive no benefit at all. This is also most likely to happen to low income workers.

Additionally, equity considerations arise because of the current exclusion. Some state and local employees have worked in Social Security covered employment and gain a Social Security benefit with a smaller contribution than other beneficiaries. Although their benefits are reduced, this reduction may be smaller than the "break" they get by paying less in payroll taxes.

AARP recommends that the committee consider mandating Social Security coverage for all uncovered state and local employees as well as any currently uncovered ones. We believe that the decision in Garcia vs. San Antonio Metropolitan Transit Authority puts the constitutional issue to rest. However, in order to ease the financial and administrative burdens on the affected jurisdictions, coverage could be phased-in by only requiring newly-hired persons to be covered initially.

- Eliminate Retroactive Benefits for Certain Beneficiaries

In general, people who get reduced Social Security benefits before age 65 cannot get retroactive benefits. However, in four distinct situations the law permits retroactive benefits. Two of the instances are (1) in order to charge off excess earnings under the retirement test, and (2) when the dependents of a worker eligible for a retroactive benefit are entitled to unreduced benefits. The Senate has passed a provision to eliminate these two exceptions.

In the first exception, a worker may charge off up to six months (in a calendar year) of excess earnings for months immediately preceding the month of filing. By so doing persons with earnings above the amount allowed by the retirement test can get benefits several months before they had actually planned on retiring. In a sense, they are avoiding the retirement test.

The dependents provision applies only to those dependents who themselves are eligible for an unreduced benefit. While children and disabled adult children receive unreduced benefits, in order for a spouse to qualify for an unreduced benefit he or she must be 65.

AARP would support repeal of these specific provisions as a means of offsetting part of the costs of liberalizing the earnings limit. These retroactive benefits represent a very small portion of all the benefits awarded. Last year out of 1.6 million new beneficiaries only 75,000 workers and 25,000 dependents were able to take advantage of these exceptions.

It applies only in very limited circumstances. Those born at the beginning of the year cannot really take full advantage of the provision. Additionally, the applicant can take advantage of the provision only if he or she knows about it or is advised of it by an SSA employee, and not all employees alert applicants to it. Since most applicants are not expecting to receive this benefit, it is more like a windfall to them.

Finally, if workers cannot receive such retroactive benefits, then their initial benefit amount will be higher. This may prove to be as advantageous as getting a lump sum and having permanently reduced benefits.

(The following options are less desirable than the preceding ones. However, they are being included because they have been proposed by CBO and the Office of the Inspector General.)

- Eliminate Social Security Benefits for Some Children of Early Retirees

One option listed by CBO to raise revenue is the elimination of Social Security benefits for children of retirees aged 62 to 64. Under current law, unmarried children of retired workers are eligible for Social Security dependents' benefits as long as they are under age 18, or attend elementary or secondary schools and are under age 19, or if they become disabled before age 22. (A child's benefit is equal to one-half of the parent's basic benefit, subject to a dollar limit on the maximum amount receivable by any one family.)

This age 18 threshold contrasts with the "in her care" benefit which has a threshold of age 16. The "in her care" benefit is given to an individual caring for the dependent child up to age 16 of a retired, disabled or deceased worker.

While AARP believes that the CBO proposal to eliminate children's benefits entirely is too harsh, some benefits adjustment, such as conforming this benefit to the age 16 "in her care" threshold, could be considered as a source of funding for liberalizing the earnings limit. However, any changes should exempt disabled adult children.

- Recoup Certain Social Security Overpayments Through Income Tax Refund Offsets

The Office of the Inspector General (OIG) has proposed recouping certain Social Security overpayments from 1979 through 1987 by an offset of personal income tax refunds. These overpayments are not those waived for hardship, rather they are ones written off as uncollectible through existing procedures.

Although OIG estimates the first year revenue gain at $216 million, CBO believes the actual figure would be closer to $100 million in 1990 and only if the proposal were fully implemented in 1989 tax year. CBO believes that OIG's second year estimate of $23 million is too low, especially if post 1987 overpayments are also recouped.

AARP recognizes that this proposal has considerable administrative costs. Also, the relationship between the Social Security Administration and the Internal Revenue Service has been a checkered one. On the other hand, the money being collected is already owed to the trust funds and could be used to help offset the costs of liberalization.

VII Conclusion

AARP believes a liberalization of the earnings limit for persons age 65 through 69 would improve the lives of many worker/retirees. Also, it represents good labor, economic and social policy for an increasingly older society. We recognize that any liberalization must have offsetting revenues, and we are prepared to work with the committee to design a reasonable proposal. We urge Congress to move ahead on this issue.

Chairman Jacobs. Mr. Pollack.

STATEMENT OF RONALD F. POLLACK, EXECUTIVE DIRECTOR, VILLERS ADVOCACY ASSOCIATES

Mr. Pollack. Thank you, Mr. Chairman. We share the concern of many Members of Congress regarding the decrease in labor force participation among our Nation's senior citizens. Between 1950 and 1986, workforce participation of older Americans age 65 and over dropped from 26.7 to 10.9 percent. This represents a terrible loss to our Nation's productivity and to our older citizens, who often find that retirement falls short of the American dream.

We believe that policies should be implemented to encourage older Americans to remain in the labor force. However, liberalizing the earnings test or eliminating the earnings test is the wrong direction to pursue, in our judgment.

There are several reasons for our position on this issue. First, it is important to understand that very few beneficiaries are affected by the earnings test. In 1986, fewer than 1 in 10 people age 65 through 69 who were eligible for Social Security benefits were affected by the earnings test.

Moreover, most of those who are affected have higher than average family incomes. Only about one-eighth of all beneficiaries between the ages 65 through 69 had family incomes above $42,000 in 1986. However, more than 40 percent of those affected by the earnings test had incomes in 1986 above $42,000. By contrast, nearly 40 percent of all beneficiaries in the age group had incomes below $15,000 and of those with incomes below $15,000, only 5 percent had earnings above the earnings limit.

If the earnings test were liberalized, most of the gains would go to people with family incomes many times higher than the poverty threshold, and this is important in light of your observations from the hearings two days ago.

According to CBO's figures for 1986, at least 72 percent of the people who would benefit have incomes greater than three times the poverty line; that is, greater than $15,800 for a single person and $19,900 for a couple.

Data is unavailable for the percentage of additional benefits that would go to beneficiaries in different income groups if the earnings test were repealed. Now, to the extent that the committee is interested in the equitable distribution of new spending of Social Security benefits—and, obviously, we argue that you should be, and I believe you are—this information should be gathered before you move forward on any of these proposals.

However, we do know that if the earnings test were repealed, eligible nonbeneficiaries who presently have high earnings would receive significant benefits. Before Congress makes any changes in the retirement test, it is important to examine the distributional impact of additional benefits.

Second, the change in the earnings test would have a significant impact with respect to Gramm-Rudman-Hollings. New spending in Social Security at this point competes in the budget resolution with other social priorities.

When Congress sets its budget targets to bring the deficit under control, liberalizing the earnings test competes with other high-priority objectives. In this year's conference on the budget resolution, for example, Congress considered what to do with respect to the Armstrong amendment and what to do with respect to changes in the Medicaid Program for lower-income seniors and children.

It turned out, to no small measure, that the proposal to liberalize the earnings test did have a competitive impact on proposed changes in the Medicaid Program—proposals that are extraordinarily important for the people you were talking about earlier in the hearing, those people with incomes, say, at $4,000.

Among low-income beneficiaries, liberalizing the earnings test would have no impact on their labor force participation rates. Low-income beneficiaries could be earning up to $8,880 now, but a variety of factors discourage them from seeking employment. These include health problems, lower educational levels, a history of intermittent employment, and dependent care responsibilities.

In 1977, as you pointed out with several of the other witnesses, Congress did increase the earnings limit. It first increased it from $3,000 to $4,000, and then in successive annual increments by $500 each. These changes had a largely insignificant impact on the labor force participation rates of beneficiaries.

Liberalizing the earnings test could increase the work effort among a small group, about 1.1 percent of beneficiaries with earnings in the middle of the earnings distribution, who deliberately hold down their earnings or hours of work to avoid the penalty.

However, there is presently no evidence to indicate that new moderate-income beneficiaries would reenter the labor market if the earnings test were liberalized. In essence, therefore, we believe that this is a misplaced priority at this point.

Chairman Jacobs. Thank you, Mr. Pollack.

[The statement of Mr. Pollack follows:]

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Testimony by

Ronald F. Pollack
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before the

SUBCOMMITTEE ON SOCIAL SECURITY
COMMITTEE ON WAYS AND MEANS
U.S. HOUSE OF REPRESENTATIVES

Washington, D.C.
Thursday, May 25, 1989

Mr. Chairman and members of the Subcommittee, thank you for inviting me to testify before you today as part of this important hearing on the social security earnings test.

Villers Advocacy Associates seeks to represent low- and moderate-income senior citizens. From our perspective, the present system is a relatively good one. The earnings test makes it possible for those low- and moderate-income beneficiaries who do remain in the labor force to augment their social security benefits with earnings. However, it does not allow upper-income older persons to continue earning a high salary and collect social security benefits at the same time.

Recently, various proposals have been developed calling for liberalizing the earnings test. Some proponents of liberalizing the earnings test have proposed raising the figure for 1990 by about $1000. Others have proposed raising the figure by $3000 in 1990, by another $3000 in 1991, and by an additional $3000 in 1992, and eliminating the limitation entirely by 1995. These proponents have proposed offsetting a portion of the cost of this increase by repealing the retroactive benefit provision available to certain categories of beneficiaries.

We believe it is not in the country's interest, particularly in our current fiscal crisis, to support the recent proposals for liberalizing the earnings test. There are several reasons for our position. First, most of those who would benefit directly from these modifications have relatively high earnings. Second, there is little evidence that these modifications would encourage low- and moderate-income older persons to reenter the labor force, and the additional benefits received by higher income seniors would have a negligible impact on their employment efforts. Third, these proposals are too costly; any additional spending should focus on the most needy of senior citizens.

Let me consider each of these arguments in turn:

Most of those who would benefit from modification of the earnings test have higher-than-average family incomes:

A recent report from the Congressional Budget Office showed that fewer than one in ten people aged 65 through 69 who are eligible for social security benefits are affected by the earnings test. [This included people aged 65 through 69 whose benefits were reduced or completely withheld in 1986 or who did not apply for benefits as a result of the earnings test.]

Most of those between the ages of 65 and 69 who were affected by the earnings test in 1986 had higher-than-average family incomes. Only about one-eighth of all beneficiaries aged 65 through 69 had family incomes above $42,000 in 1986. However, more than 40 percent of those affected by the earnings test had incomes above $42,000. By contrast, nearly 40 percent of all beneficiaries aged 65 through 69 had incomes below $15,000. Of those with incomes below $15,000, only 5 percent had earnings above the exempt limit. (See Figure 1)

Further evidence that the earnings test affects primarily those who are economically better off is found by measuring income relative to poverty thresholds. In 1986, the poverty threshold for a single person aged 65 or over was $5,255. For a two-person family headed by a person aged 65 or over, the poverty threshold was $6,630.

In 1986, beneficiaries with family incomes above four times the poverty threshold made up just over one-fourth of all beneficiaries between the ages of 65 and 69. However, they constituted nearly three-fourths of those affected by the earnings test. Conversely, those with incomes below twice the poverty threshold represented one-third of all beneficiaries between the ages of 65 and 69. However, these beneficiaries represented barely 1 percent of those with earnings above the exempt level. (See Figure 2)

If the earnings test were liberalized, most of the gains would go to people with relatively high family incomes. According to the Congressional Budget Office, 72 percent of the people who would benefit have incomes greater than three times the poverty level -- that is, greater than about $15,800 for a single person and about $19,900 for a couple. What is not known is the percentage of additional benefits that would go to beneficiaries in different income groups. However, we do know that, if the earnings test were repealed, eligible nonbeneficiaries who presently have high earnings would increase their income. Before Congress makes any changes in the retirement test, it is important to examine the distribution of additional benefits that would result.

Modification of the earnings test would not encourage significant numbers of low- and moderate-income older persons to reenter the labor force:

Proponents of liberalizing the earnings test argue that it would lead to increased work effort on the part of senior citizens. However, there is little evidence to support this argument.

Among older persons with high income from earnings, liberalizing the earnings test could lead to increased work effort. Alternatively, liberalizing the earnings test could lead to reduced work effort among high earners as social security benefits substituted for previous earnings.

For low-income beneficiaries, liberalizing the earnings test would have virtually no impact on their labor force participation rates. Low-income beneficiaries between the ages of 65 and 69 could be earning up to $8880 a year now without jeopardizing their social security benefits. A variety of factors -- including health problems, lower educational levels, a history of intermittent employment, and dependent care responsibilities -- discourage them from seeking employment.

When previous changes were made in the earnings test, low-income beneficiaries did not return to the labor market. Under the Social Security Amendments of 1977, the annual exempt amount was raised to $4,000 in 1978 and by $500 increments in successive years, until it reached $6,000 in 1982. These changes did not increase the labor force participation rates of low-income beneficiaries.

Liberalizing the earnings test could increase the work effort of a small group of beneficiaries with earnings in the middle of the earnings distribution. These are the beneficiaries with earnings just below the limit who deliberately hold down their earnings or hours of work to avoid the penalty. They accounted for only 1.1% of beneficiaries in 1980.

When the exempt amount was raised in 1977, some beneficiaries with earnings near the exempt amount did increase their hours of work and earnings. If the earnings limit were raised, it is reasonable to assume that some of the small number of beneficiaries with earnings near the annual exempt amount would increase their work effort correspondingly. However, there is presently no evidence to indicate that new moderate-income beneficiaries would reenter the labor market if the earnings test were modified. Before taking any action, we urge Congress to undertake an analysis of the likely behavioral changes that would result from liberalizing the earnings test.

Liberalizing the earnings test would cost billions of dollars:

The cost over five years of liberalizing the earnings test by $1000 increments is $1.2 billion. The five-year cost of increasing the figure in $3000 increments is $6.3 billion.

Proponents of liberalizing the earnings test have proposed offsetting a portion of the cost of this increase by repealing the retroactive provision in the Social Security system. Under current law, some categories of retirees can collect up-front a lump sum benefit equal to six months of their benefits in exchange for lower payments over the balance of their lifetimes. Proposals to repeal the retroactive provision would affect two categories of beneficiaries. The first category includes beneficiaries with a spouse who is collecting unreduced benefits -- that is, the higher benefits granted to beneficiaries who wait to apply for Social Security until age 65. The second category of beneficiaries who would be affected are those with pre-retirement earnings over the amount allowed under the retirement test.

The proposal to repeal the retroactive provision represents a significant cut in benefits for some beneficiaries. The fairness of this proposal is in question: It would pay for increased benefits for beneficiaries who continue to work by cutting benefits for beneficiaries who are no longer in the labor force. Before taking action, we urge Congress to examine the distributional impact of this proposal.

In addition, the savings resulting from repealing the retroactive provision is only $0.8 billion. This represents only a portion of the cost of liberalizing the earnings test. Proponents of liberalizing the earnings test argue that the additional costs would be largely offset by the increased income and payroll taxes paid by retirees who reenter the labor force. However, the Social Security Administration estimates that new revenues would offset only 10 percent to 15 percent of the additional outlays required. If the Social Security Trust Fund is to remain in balance, an increase in the Social Security tax would be required to pay for modifications in the earnings test.

As costly initiatives, modifications in the earnings test could fuel a backlash against social security. If it came to light that older people earning $50,000 salaries were also collecting social security benefits, this could give legitimacy to social security's critics. It might lead to increased interest in limiting benefits for the middle class and the wealthy and jeopardize benefits for low-income beneficiaries as well.

Rather than spend billions of dollars on liberalizing the earnings test, we urge Congress to target resources toward the most needy. One alternative would be to increase funding for the Title V Community Service Employment Program. This program provides part-time community service jobs for approximately 62,000 low-income older workers. The current federal spending for this important employment program is only $336 million. By doubling the federal commitment to the Title V program, many more low-income people could gain access to paid employment.

A second alternative would be to make changes in Social Security and Supplemental Security Income that would benefit our poorest elders. The number of older persons with incomes below the poverty line is 3.5 million. As of 1987, poor elderly households received 70 percent of their income from Social Security and 11 percent from public assistance (AFDC, SSI, or general assistance). Still, our poorest elders have only a fifty percent chance of receiving income assistance equal to 74 percent of the poverty line.

One proposal is for Congress to modify the monthly earned income disregard for SSI beneficiaries. Under current law, the first $65 of monthly earned income plus one-half of remaining earnings is disregarded for SSI beneficiaries. One-half of the remaining earnings is counted as "countable income" and SSI benefits are decreased accordingly. Essentially, SSI beneficiaries are subject to a 50 percent reduction ratio on earnings above $65 a month. Increasing the earned income disregard would bring some SSI beneficiaries up to the poverty level.

In addition, Congress could create a minimum Social Security benefit that takes into account total income. Extending such a guarantee involves complex fiscal and jurisdictional considerations. We hope this committee will nevertheless keep that goal within its sight. From an equity perspective, increasing SSI and Social Security benefits for our poorest elders makes more sense than increasing benefits for more affluent elders through liberalizing the earnings test.

Conclusion

Liberalizing the earnings test would not be in the interest of most older persons. Those who would benefit are primarily individuals with relatively high incomes. Increasing their benefits would be an unjustified allocation of limited resources.

Congress has already instituted one costly change in the social security earnings test. Under current law, the benefit reduction ratio in 1990 will be reduced from 50 percent to 33.3 percent for beneficiaries between the ages of 65 and 69. Social security actuaries estimate that this change will cost approximately $1 billion a year in increased outlays. These costs are not justified. Those most likely to benefit are higher-income beneficiaries who would have remained in the labor force, with or without the changes.

Before taking any action, Congress should carefully examine the distributional and fiscal impact of both the current earnings test and any proposals for modifying it. Congress should also consider reversing or modifying the reduction in the benefit reduction ratio due to go into effect in 1990. It would certainly be unwise and premature to implement further modifications in the social security earnings test without first undertaking a serious assessment of the costs and the benefits.

FIGURE 1. DISTRIBUTION IN 1986 OF PEOPLE AGED 65-69 ELIGIBLE FOR SOCIAL SECURITY BENEFITS AND AFFECTED BY THE EARNINGS TEST, BY FAMILY INCOME

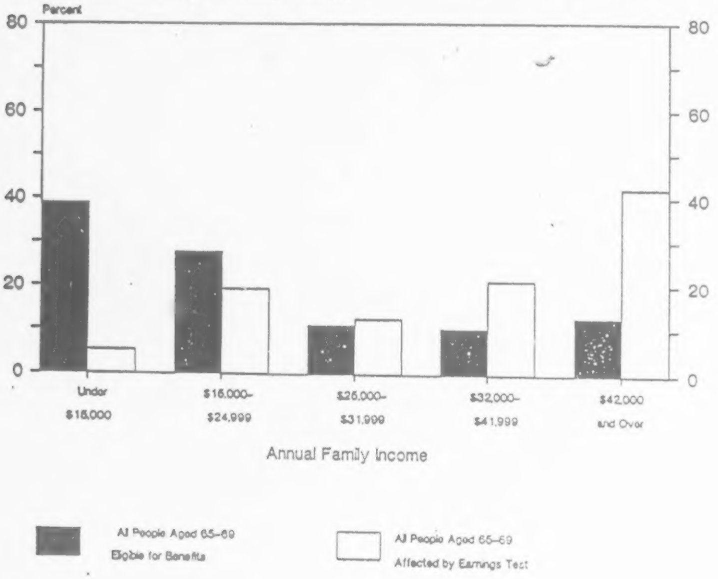
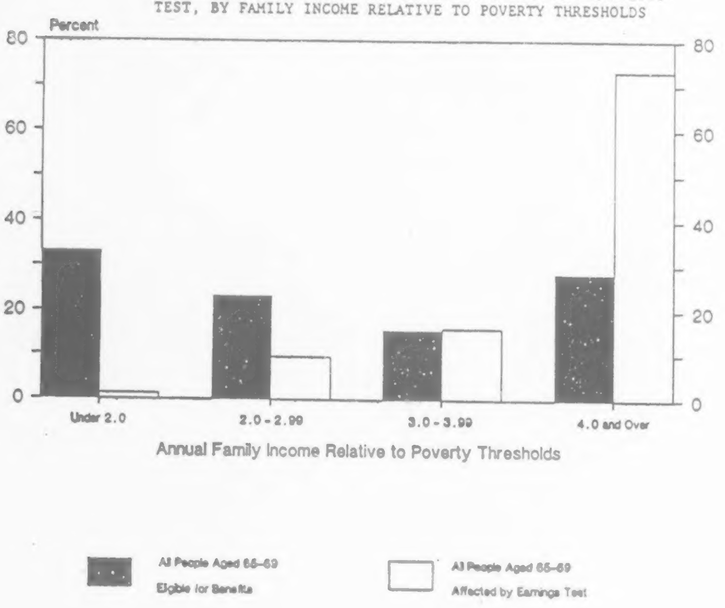


FIGURE 2. DISTRIBUTION IN 1986 OF PEOPLE AGED 65-69 ELIGIBLE FOR SOCIAL SECURITY BENEFITS AND AFFECTED BY THE EARNINGS TEST, BY FAMILY INCOME RELATIVE TO POVERTY THRESHOLDS



SOURCE: Congressional Budget Office tabulations of data from the March 1987 Current Population Survey.

Chairman Jacobs. Mr. Myers.

STATEMENT OF ROBERT J. MYERS, FORMER CHIEF ACTUARY, SOCIAL SECURITY ADMINISTRATION

Mr. Myers. Thank you, Mr. Chairman. First, I would like to say a few words about life expectancy, retirement ages, and Bismarck, and to correct the record a bit. I would not dare to do this, Mr. Chairman, if I did not think that we were such good friends, and also if I did not think that paramount in your interest are the facts.

Chairman Jacobs. Mr. Myers, if I bum-rapped Bismarck, I apologize abjectly.

Mr. Myers. The fact, Mr. Chairman, is that, when Social Security was enacted in 1935, life expectancy was about 64 years. That, of course, did not mean that everybody lived to age 64 and then died, and that nobody got benefits.

Rather, life expectancy of age means that one-half of the babies born will live to age 64, and the one-half who live to age 64, at that time, will live for about 12 additional years.

Finally, about Bismarck, strange as it may seem, 100 years ago when Bismarck developed the German social insurance system—the first in the world—age 70 was selected as the retirement age, not age 65.

You will hear this figure quoted as age 65 very widely, but I assure you that it was age 70. I have the original German law and that is the correct figure.

Chairman Jacobs. Yes. The Washington Post is forgiven.

Mr. Myers. This is a battle that our good friend, the late Wilbur Cohen, and I fought for years. Bismarck chose age 70.

Chairman Jacobs. OK.

Mr. Myers. Thank you, Mr. Chairman.

Chairman Jacobs. That is definitely on the record now.

Mr. Myers. For many years, I have favored the retirement test under Social Security because of the simple fact that you do not pay retirement benefits to people who are not retired.

I never went along with the argument that people paid their contributions for a benefit at age 65—just as you too have stated, Mr. Chairman as not being the case—and that they should get benefits at that point. What they were "buying" was a retirement pension when they reached age 65 and retired from substantial gainful work.

This is a very fine theory, but in the last few years I have changed my mind about it because, in practice, the phased-in retirement test that we now have creates imponderable disincentives for work for people earning roughly $10,000 to $30,000 a year.

As has been stated, people in that area of earnings, after taking into account Social Security taxes; State, local, and Federal income taxes; work expenses; the catastrophic Medicare premium; and so forth, will take home only perhaps 10 to 20 percent of their actual earnings above the exempt amount. In fact, there are cases where people actually lose money by working.

Some of us that have nice jobs, like Members of Congress and actuaries, are willing to work for virtually nothing. We like to work.

But the great majority of the American population, in my opinion, is not going to work if they could only take home 10 percent of their salary.

Let me say a few words about the delayed retirement credits. When they get up to 8 percent, as present law schedules it, they will be about the actuarial equivalent. So, just like with an insurance company, a person can take an annuity at age 65, or can take a higher one later. The insurance company does not care. On the average, it will balance out if the amounts available for retirement at various ages are actuarially equivalent. When the DRC's become 8 percent, they will be almost actuarially equivalent—about 9 percent would probably be a more nearly equivalent figure.

What I would propose is that the retirement test should be eliminated after age 65. The 8-percent DRC's ought to be available at once, and—this is a very important part of my proposal—there should be an intensive educational campaign by the Social Security Administration, which should give advice to people and point out why they should not take the benefits at age 65 in many cases, and why the DRC's might be better.

Let me give an example. One reason that deferring benefit receipt and getting DRC's is better is that then there is a better spread of income. Another reason is that persons may pay more taxes if they take their benefits right away at age 65.

Let us take a single person earning $25,000 with an $8,000 Social Security benefit at age 65. If that person claims benefits and works on for 3 years, he or she will have $33,000 of income per year for 3 years; then it will drop off to $8,000. That is not good economic planning.

On the other hand, if the person does not take the benefit until the end of the 3 years, he or she will have $25,000 per year for the first 3 years and then will have $10,000 a year. So there will be a much better economic distribution picture that way.

Furthermore, in this case, if the person takes the benefit of $8,000 when age 65, income taxes will be paid on it, and the person will lose perhaps as much as one-third of the benefit through Federal income taxes. On the other hand, if he or she waits until 68 and takes the $10,000 benefit, income taxes will not be paid on it.

What about very high-income people, those who make $100,000 or more a year? I believe that those people should not get benefits, even if they are not smart enough to know that it is better to wait and take the higher benefits based on the DRC's?

To prevent this, I would impose higher income taxes on them than merely having the present 50 percent of benefits be taxable. It would be phased in, as I have stated in my testimony. This would discourage them from taking benefits at age 65 and, instead, to do what really is the proper thing of taking the deferred benefits with the DRC's.

In closing, Mr. Chairman, I would like to suggest that, if we can afford to eliminate the retirement test from a cost standpoint in 2009 and thereafter—when the baby boomers are coming along to retirement with their higher costs—we can afford to do it now by putting the 8-percent delayed retirement credits into effect immediately.

Some cost-reduction changes can be made to compensate for this change. For instance, I would eliminate child's benefits for workers who retire early, at ages 62 to 64. I think that it is a mistake to have child's benefits payable for them. But, again, this is a matter that should be given more study.

The last thing that I would say is that, if the retirement test is not eliminated, the better thing to do is not to raise the annual exempt amount—as many have proposed—but rather to leave the exempt amount the way that it is and instead have smaller reductions for "excess" earnings. The $1 for $3 reduction that will be effective next year might better be $1 for $4 or even $1 for $5.

Thank you, Mr. Chairman.

Chairman JACOBS. Thank you, Mr. Myers.

[The statement of Mr. Myers follows:]

STATEMENT BY ROBERT J. MYERS PRESENTED TO THE SUBCOMMITTEE ON SOCIAL SECURITY OF THE COMMITTEE ON WAYS AND MEANS, HOUSE OF REPRESENTATIVES, MAY 25, 1989, WITH REGARD TO THE SOCIAL SECURITY RETIREMENT TEST.

Mr. Chairman and Members of the Subcommittee: My name is Robert J. Myers. I served in various actuarial capacities with the Social Security Administration and its predecessor agencies during 1934-70, being Chief Actuary for the last 23 of those years. In 1981-82, I was Deputy Commissioner of Social Security, and in 1982-83, I was Executive Director of the National Commission on Social Security Reform.

The retirement earnings test under the Old-Age, Survivors, and Disability Insurance program has, over the years, attempted to draw a line between being retired and being employed. In the original Act, this provision was on an "all or none" basis, in that benefits were to be withheld for persons who engaged in "regular employment" (not defined in the law). This concept was changed somewhat in the 1939 Act, before monthly benefits first became payable, so as to establish covered wages of $15 per month as the point at which the person was not considered retired, and therefore no benefits were payable.

Over the years, the earnings test has been changed so as to phase in more smoothly and equitably for persons who have moderate earnings. At present, there is an annual exempt amount -- currently, $8,880 for persons aged 65 - 69 and $6,480 for younger persons -- such that persons with earnings equal to or less than this receive full benefits, whereas those with higher earnings have their benefits reduced by $1 for every $2 of excess earnings, on a $1-for-$3 basis in 1990 for persons at and above the Normal Retirement Age (currently, 65).

Originally, the earnings test applied at all ages. The 1950 Act provided that it should not be applicable after attainment of age 75. Such limiting age was reduced to 72, effective for 1955, and then to 70, effective for 1983. In all logic, there is no reason to have a limiting age beyond which the test does not apply. This basis was adopted solely because of political pressures arising from individuals who argued that, otherwise, they would never get any return on their contributions because they would work all their lifetime.

Individuals who have benefits withheld because of excess earnings are compensated therefor, as to OASDI benefits, through two means. First, the additional earnings result in a recomputation that may increase subsequent benefit amounts -- but this will not always occur, depending upon the current level of earnings as contrasted with that in previous years. Second, future benefits are increased by the Delayed Retirement Credit (DRC), which is at the rate of 3% per year for those who attain age 65 in 1982-89 (1% for those attaining age 65 earlier), but will increase gradually for persons reaching age 65 later. In the long run, the DRC will be at the rate of 8% per year -- for those attaining the Normal Retirement Age in 2009 (when it will be age 66) and thereafter.

It is important to note that, when the DRC is 8%, it will then be approximately the actuarial equivalent. By this is meant that, insofar as the OASDI program is concerned, the long-range cost effect of persons delaying retirement and then receiving larger benefits due to the DRCs will be approximately the same as though benefits were payable automatically at the Normal Retirement Age, regardless of subsequent earnings. It may also be noted that this actuarial equivalency is present for those who now retire before the Normal Retirement Age. Specifically, at present, if an individual retires at age 62, the benefit is 80% of that available at age 65. Thus, if retirement were deferred for 3 years, the benefit would be 25% higher relatively, or about 8% per year of delay.

Over the years, the earnings test has been perhaps the most controversial feature of the OASDI program insofar as the general public was concerned. Many people view it as being unfair because they believe it to be a significant deterrent to continued employment -- which, as I will discuss later, is frequently actually the case. Still other persons believe the earnings test to be unfair because they believe that "they have bought and paid for the benfits to be payable at age 65" -- but this is not a correct conclusion, because the "insurance" provided was against retirement, not against attainment of age 65.

In defense of the earnings test, the basic argument is that it is not appropriate to pay retirement benefits to people who are not retired, because they are still in the paid labor market. Employers having private pension plans do not continue individuals in employment beyond the normal retirement age and pay them both salary and pension. Especially, it is argued that program costs should not be incurred in paying benefits to persons beyond the Normal Retirement Age who are earning high salaries -- often as much or more than they ever did in the past.

I believe strongly, in theory, in the principle of the retirement test. However, up to this time, despite great effort to have the test operate so as to phase in equitably between full employment and full retirement, it produces significant disincentives for employment for a large number of persons.

Quite obviously, persons with relatively low earnings -- below the annual exempt amount -- have no work disincentives on account of the test. However, those with higher earnings -- up to perhaps $35,000, or about twice the nationwide average earnings -- have very considerable disincentives. Additional work by them beyond the annual exempt amount results not only in a loss of some benefits, but also the payment of higher federal and state income taxes -- and FICA-SECA taxes as well. As a result, the net gain from additional work will be relatively small. For more specific details on this subject, may I refer to my paper "Income of Social Security Beneficiaries as Affected by Earnings Test and Income Taxes on Benefits" in The Journal of Risk and Insurance, June 1985.

As a partial offset to the small incentive to work under such circumstances, there is the favorable financial effect over the long run that larger benefits will eventually be payable when retirement occurs (or at age 70, if earlier). However, although this is a very real offsetting feature, many people so affected do not understand its effect, but rather only look at current net income and not also -- as should properly be done -- at the present value of the additional future benefits.

I am now convinced that the solution to the problems caused by the earnings test is to eliminate it for all persons at or above the Normal Retirement Age and, at the same time, to raise the DRC to 8% for all future non-payment of benefits for persons at or above the Normal Retirement Age. Further, the DRC should be made applicable at ages 70 and over, for those who wish to defer benefit receipt until they cease employment.

Simultaneously, a continuing educational campaign should be mounted to inform individuals about the advantages of deferring claim for benefits until they actually retire after the Normal Retirement Age, so that they receive the substantial increases from the DRCs. Such procedure results in much better benefit design -- namely, having only earnings while working, and a larger benefit while retired, versus a very high income while working (earnings, plus "normal" benefits), but sharply reduced income while retired ("normal" benefits only). Furthermore, such levelling of income over the years after Normal Retirement Age might produce lower income taxes over all (especially if a proposal described later is adopted).

These changes would increase the cost of the program somewhat, but this cost can readily be met by changes that I will propose. Such increased cost due to the larger DRCs will ultimately be present anyhow under present law. If we can afford it then, we can afford it now!

Actually, increasing the DRCs at once would reduce costs in the short run because individuals would be more likely to defer retirement and thus receipt of benefits.

In order to meet the cost of the proposed change over the long run -- and, at the same time, to discourage high-earnings persons from claiming benefits at the Normal Retirement Age, rather than waiting to receive the higher benefit available when they retire later -- I suggest the following change in the taxation of OASDI benefits. Individuals who have earnings (whether or not in covered employment) in the United States which are in excess of the annual exempt amount (determined as at present, and used only for this purpose) and who are entitled to benefits for all 12 months of the year and are age 65, but under age 70 in all such 12 months, would be subject to additional income tax on their benefits (which would accrue to the OASDI trust funds). This would be done by increasing the amount of their benefits otherwise subject to income tax (if any) by 100% -- but by no more than 50% of their earnings in excess of the annual exempt amount.

For example, consider an individual aged 67 who, under present law, has $6,000 of benefits subject to income tax. If he or she has earnings which are well above (i.e., at least $12,000) the annual exempt amount, the benefits subject to income tax would be increased to $12,000. On the other hand, if the earnings are only slightly above the exempt amount, the benefits subject to income tax would be only slightly increased.

Quite naturally, this would discourage what some consider the undesirable situation of high earners under age 70 simultaneously drawing OASDI benefits. This procedure, although seemingly mathematically complex, would be administratively easy and inexpensive to do.

Another change that could be made to finance the proposal is to eliminate child's benefits (and the related mother's benefits) for persons drawing reduced old-age benefits at ages between 62 and the Normal Retirement Age. It is really illogical to provide such benefits when the worker's benefit is actuarially reduced for early retirement,but these full, additional benefits are then payable. As a result, many persons are undesirably encouraged to retire early.

I believe that, over the long range, these changes would finance the temporary increase in cost that results from eliminating the earnings test at ages 65-69 and from having 8% DRCs. I say "temporary" because under present law there will be 8% DRCs eventually, and from a cost standpoint this is the same as eliminating the earnings test after the NRA then. From a cash-flow, budget situation, the combined proposal would have a small "excess outgo" situation in the early years. However, this is not important insofar as the long range is involved -- and policymaking for OASDI should be made from this perspective.

Incidentally, I believe that some statements that are made about the cost of eliminating the earnings test and having immediate 8% DRCs are misleading, or at least do not tell the full story. For example, the dollar figures cited for the cost for the next 5 years do not recognize the cost reductions later because people took benefits immediately and thus did not the receive the DRCs otherwise payable.

Some have proposed that part of the cost of eliminating the earnings test at ages 65-69 should be met by eliminating recomputations of benefits for earnings received after initial entitlement to retirement benefits. I oppose such a change. First, potential OASDI benefit rights should be available on all earnings credits for which contributions have been paid. Second, it is unfair to place persons in the position that they must decide when it is most (or least) advantageous to file claim (and the District Offices of SSA cannot, and will not, advise them on such matters). Instead, the long-standing principle should be continued that individuals are never adversely affected by early claims filing.

Another proposal is to not permit retroactive benefits for certain persons who are eligible for reduced benefits. This is probably a desirable change.

Yet another proposal is to liberalize the earnings test by increasing the annual exempt amount over what it would be under present law. If only minor changes, rather than complete elimination are to be made, I would prefer reducing the reduction proportion for earnings -- say, from the $1 for $3 basis to be effective in 1990 to $1 for $4 (to be applicable under age 65, as well as above).

Finally, let me give an example of why, if the earnings test is eliminated, many persons should defer claims for benefits and thus receive larger benefits later due to the DRCs. Suppose a single person at age 65 has a $8,000 Social Security benefit and can earn $25,000 a year for the next three years. If immediate benefits are elected, the annual income will be $33,000 for three years, and then will fall to $8,000. Would it not be much better income design to defer benefit receipt until actual retirement, and then have $25,000 of income for the first three years and then $9,920 thereafter? Furthermore, if the benefits are claimed at age 65, 50% of them will be subject to income tax, and this will increase income taxes by as much as $1,120 a year for the first three years, whereas no income taxes on the benefits would be payable if they are not claimed until retirement at age 68.

Chairman **Jacobs**. Mr. Entin.

STATEMENT OF STEPHEN J. ENTIN, RESIDENT SCHOLAR, INSTITUTE FOR RESEARCH ON THE ECONOMICS OF TAXATION

Mr. **Entin**. Mr. Chairman, thank you for the opportunity to appear. The last time I appeared before the subcommittee, I gave some illustrations of the confiscatory marginal tax rates created by the earnings test.

A married couple age 65 with $18,000 in income can face an 81-percent marginal tax rate. If subject to the taxation of Social Security benefits, the marginal rates can exceed 100 percent, and now there is the added complication due to the Medicare catastrophic surtax, which will be 28 percent by 1993. There were far better ways of handling both the taxation of benefits and the financing of catastrophic coverage.

You may hear that certain features of Social Security offset some of these negative impacts, but the recomputation of benefits, if one works extra years, and the delayed retirement credit [DRC] are very inadequate offsets at the present time.

However, the DRC is being increased in stages to 8 percent. Those reaching age 62 after the year 2005 will be able to work a few extra years and still collect full lifetime benefits. As Mr. Myers has explained, this will send the cost of repealing the earnings test to zero. So this is not a cost that would grow over time. It is strictly a transitory cost, and it would be very well accompanied by an acceleration of the 8-percent delayed retirement credit to the present.

You have asked for suggestions regarding financing of repeal or liberalization of the earnings test. Repeal of the earnings test is most often discussed for those ages 65 through 69, for whom complete repeal would cost about $5 billion per year in higher outlays before offsets.

About one-half of this cost might be recovered through higher income and payroll taxes due to higher earnings under reasonable assumptions. CBO and others dramatically underestimate this effect.

However, whatever one estimates is the effect, your staffs will not allow you to count these reflows under current budget-scoring rules. I think that is unfortunate. However, about $0.1 to $0.2 billion might be recovered automatically from income taxation of the additional benefits paid out under current income tax treatment. The latter would be counted under budget-scoring rules.

In addition, minor adjustments to the benefit computation process that have been considered at one time or another by SSA and the Congress might be employed to provide additional savings.

For example, accelerating the already scheduled increase in the delayed retirement credit to 8 percent in 1989, eliminating the recomputation of benefits for additional earnings after reaching normal retirement age, and elimination of two exceptions to the rule prohibiting retroactive entitlement in reduced benefit cases, would save about one-third of the cost of repeal, and that would include the administrative cost savings of about $0.1 billion.

There would be benefit from considering a phase-in of the reform, which could make the task even easier. Assuming no offsets or tax reflows, eliminating the test for those age 69 in 1990, age 68 in 1991, and so on, in stages, would obviously soften the impact.

During this period, normal real economic growth will be raising real Federal revenues by about $30 billion each year, and this reform would then take only a bit over 3 percent of the real growth of Federal revenues over 5 years.

The committee might also consider accelerating another provision that is already in current law. I refer to the scheduled increase in the normal retirement age. The 1983 Social Security amendments provided for an increase from 65 to 67 in the normal retirement age.

The age will rise from 65 to 66 at a rate of 2 months per year for those reaching age 62 between the years 2000 and 2005. It will rise from 66 to 67 for those reaching age 62 between 2022 and 2027.

Accelerating the current law retirement age increases by 10 years to begin the increase in 1990 would save enough in outlays to cover half the cost of repealing the earnings test by 1995.

The rise in retirement age is very gradual. Someone turning age 62 in 1990 and planning to retire at age 65 in 1995 would have to plan on working two additional months in 1995 to collect full benefits.

Someone planning on retiring early at age 62 in 1990 could choose between two additional months of work or an additional early retirement penalty of less than 1 percent of the primary insurance amount.

Much will undoubtedly be made over the distribution of benefits across income classes from repeal of the earnings test. I would just urge you to note that upper income beneficiaries will pay far higher taxes on the benefits than others, and this is certainly not the provision through which you want to handle progressivity issues in the income tax.

Thank you.

Chairman JACOBS. Thank you.

[The statement of Mr. Entin follows:]

Statement of Stephen J. Entin
Institute for Research on the Economics of Taxation

before the

Committee on Ways and Means
Subcommittee on Social Security

Hearing on Modification of the Social Security Earnings Test

May 25, 1989

The social security retirement earnings test is damaging to the economy, hurts elderly workers financially and infringes on their personal liberty, and is immensely unpopular. It should be possible to find an acceptable schedule for the gradual elimination of this provision within budget constraints.

How the test operates.

The earnings test reduces social security benefits by $1 for every $2 of wage and salary income earned by a beneficiary above exempt amounts. In 1989, the exempt amounts are $6,480 for beneficiaries under age 65, and $8,880 for beneficiaries age 65 through 69. Those over age 69 are not subject to the earnings limitation. The rate of benefit reduction is scheduled to fall to $1 for every $3 of excess earnings in 1990, but only for beneficiaries at or above normal retirement age, currently 65. As the normal retirement age is raised from 65 to 66, and from 66 to 67 in stages for people reaching age 62 between the years 2000 and 2005, and 2022 and 2027, respectively, the reduction will revert to $1 for every $2 of excess earnings for those ages 65 and 66.

Effect on marginal tax rates.

The $1 for $2 benefit reduction is equivalent to a 50 percent marginal tax rate on a beneficiary's earnings in excess of the exempt amounts, until the excess earnings build to more than twice the social security benefits and all benefits have been lost. (Even the pending $1 for $3 benefit reduction will impose a 33 percent add-on tax rate, over earnings equal to three times the benefits.) On top of this must be added other tax rates facing the working beneficiary. The most obvious among these are the marginal federal and state income tax rates and the payroll tax rate. In addition to these basic tax rates, there are also large increases in marginal tax rates for many Social Security beneficiaries due to the phase-in of income taxation of benefits and to the income tax surcharge implicit in the catastrophic coverage provisions of Medicare, discussed below. (Other taxes or tax-like disincentives not factored into this analysis include federal and state unemployment taxes and welfare benefits subject to phase-out with income.)

When the various basic taxes are imposed together, marginal tax rates can become very high at moderate income levels. A married couple age 64 with total income of $10,000 could face a 65 percent marginal tax rate. A couple age 65 with income of $18,000 could face a marginal tax rate of 81 percent. At higher incomes, with all benefits lost, the marginal rates would be lower.

BASIC TAX RATES UNDER THE EARNINGS TEST

	single retiree	married couple	
	age 65	age 65	age 64
income from:			
pension	$ 1,000	$ 1,000	$ 0
savings	1,000	1,000	0
wages	8,900	8,900	6,500
social security	6,000	8,000	4,000
total income	$16,900	$18,900	$10,500
tax on added dollar of wage income from:			
benefit reduction	50%	50%	50%
federal income tax	15	15	0
payroll tax (self-empl.*)	13.02	13.02	13.02
state income tax	3	3	2
total marginal rate	81.02%	81.02%	65.02%

* The examples incorporate the 1989 self-employed payroll tax rate, 15.02 percent less a 2 percent credit, or 13.02 percent. This is close to the combined employer-employee rate after allowance for deductibility of the employer's share. The combined rate is the true measure of the tax burden on the gross wage.

Interaction with income taxation of social security benefits.

As taxpayers move toward the upper end of the 15 percent tax bracket or the bottom of the 28 percent tax bracket, most would have sufficient social security income to trigger taxation of benefits. Their added wage income would then be subject to both the earnings limitation and the effects of benefit taxation.

Taxation begins when the sum of a beneficiary's adjusted gross income, tax exempt bond income, and half of social security benefits exceed $25,000 for a single beneficiary and $32,000 for a married couple filing jointly. These amounts are not adjusted for inflation, and will affect more beneficiaries each year at lower real incomes. For each dollar by which this sum exceeds the exempt amounts, $0.50 of the taxpayer's social security benefit becomes taxable income, up to half of benefits. During this phase-in range, the effect of earning an added dollar of interest or wages is to increase taxable income by $1.50, effectively raising the marginal tax rate on the added dollar of wages or interest by half, e.g., from 15 percent to 22.5 percent or from 28 percent to 42 percent. This is an unfortunate tax penalty on private saving for retirement.

Sheltering of lower income taxpayers from taxation of benefits could be achieved quite simply, and without this tax "spike" and interactive penalty on other retirement income, by an alternate method of benefit taxation. Some amount of benefits, say, $4,000 for a single retiree, $6,000 for a couple using a 50 percent spousal benefit, and up to $8,000 for a couple with independent benefits, could be made tax exempt. Benefits above the exempt amounts would be taxable, up to half of benefits.

When a beneficiary is subject to both the earnings test and the phase-in of benefit taxation, the interaction of the two provisions produces an effective increase of 37.5 percent in the marginal tax rate on wage and salary income, rather than one-half. (The added dollar of wages costs the beneficiary $0.50 in benefits, half of which applies toward the threshold of benefit taxation. The net result is an additional $0.75 in income above the threshold, and an additional $0.375 in taxable benefits. Thus, the consequence of the added dollar of wages is to raise taxable income by $1.375.) This effectively raises the 15 percent tax rate to 20.625 percent, and the 28 percent tax rate to 38.5 percent. Marginal tax rates under these conditions can exceed 100 percent.

TAX RATES UNDER THE EARNINGS TEST AS BENEFITS BECOME SUBJECT TO TAX

	single retiree age 65	married couple age 65
income from:		
pension	$9,000	$12,000
savings	5,000	7,000
wages	8,900	8,900
social security	8,000	12,000
total income	$30,900	$39,900
tax rate on added dollar of wages from:		
benefit reduction	50%	50%
federal income tax	38.5	38.5
payroll tax (self-employed)	13.02	13.02
state income tax	4	4
total marginal rate	105.52%	105.52%

Interaction with the Medicare Catastrophic Surtax.

The Catastrophic Coverage Act of 1988 imposes an income tax surtax on all those eligible for Medicare (whether enrolled or not) to finance additional Medicare benefits. The surtax will be 15 percent in 1989, rising to 28 percent in 1993. This has the effect of adding another 4 to 8 percentage points to the marginal federal income tax rates of those eligible for Medicare who are not at the maximum catastrophic tax. (The surcharge is capped at $800 for a single taxpayer and $1600 for a married couple filing jointly in 1989, rising to $1050 for a single filer and $2100 for joint filers in 1993.) For those affected, the marginal tax rate in the 15 percent bracket will effectively become 17.25 percent in 1989 and 19.2 percent in 1993; the marginal tax rate in the 28 percent bracket will become 32.2 percent in 1989 and 35.84 percent in 1993.

Taxpayers who are experiencing the phase-in of taxation of social security benefits are generally in the 28 percent tax bracket, which is kicked up to 38.5 percent by the interaction of the phase-in and the earnings test. For these taxpayers, the Medicare surcharge will lift the marginal income tax rate to 44.275 percent in 1989 and to 49.28 percent in 1993. In future years, people in the 15 percent bracket will become subject to taxation of benefits, as the unindexed thresholds fall in real terms. They will also face the 28 percent surcharge (or even higher rates if these prove inadequate to cover catastrophic outlays), for a combined effective rate of 26.4 percent. To these marginal income tax rates would be added the 50 percent or 33 percent earnings limitation tax, depending on the year, and the payroll and state and local income taxes, for combined rates well above those just described.

Effect of Recomputation of Benefits.

Working additional years may increase one's earnings history and result in an automatic increase in one's Social Security benefit. This may offset a part, but generally only a small part, of the high tax burden on the earnings subject to the earnings test.

Effect of delayed retirement credit (DRC).

Those retiring later than the month of attaining age 65 have their benefits increased by 1/4 percent per month for each month retirement is delayed past age 65. Those whose benefits are reduced in any month by the earnings test receive an increase in their future benefits of a similar 1/4 percent for each month the earnings test applied, beginning once their earnings have dropped below exempt amounts. Some may claim that this provision relieves the damage to incentives done by the earnings test. In fact, the DRC is not an adequate offset to the adverse effects of the earnings test.

The DRC acts as a partial offset to the incomplete indexation of workers' earnings histories in determining initial retirement benefits (primary insurance amounts, or PIA's). A retiring workers' earnings are indexed up until age 60. These indexed earnings are added to unindexed earnings through age 62, 65 or any later retirement age in determining average lifetime earnings and PIA's. Furthermore, any earnings after retirement which go into a recomputation of benefits are not indexed. Thus, delayed retirement means giving up indexation of a larger portion of the wage history, resulting in lower replacement rates the longer one delays retirement. The DRC at current levels is a partial adjustment for that problem.

The current DRC is not adequate on an actuarial basis to make the present value of expected lifetime benefits under delayed retirement equal to the expected benefits received by retiring at age 65 (or age 62, in spite of the ERP). Under current law, the DRC is being increased in stages to 2/3 percent per month for those reaching age 62 in 2005 and beyond. This will make the annual increase in benefits from delayed retirement equal to 8 percent per year. Under current interest rate and life expectancy assumptions, this should make the present value of expected benefits equal whether one retires at age 65 or later.

This would go a long way toward removing the disincentive from the earnings test. One could work several extra years and still collect the same lifetime benefits. The earnings test would then cease to affect the amount of benefits paid, and influence only their timing. The earnings test could then be eliminated for those 65 and over with no meaningful budget consequences. However, this is seventeen years away, and does nothing to address the current problem.

Note that the rise in the DRC means that, as compared to current law, the cost of repealing the earnings test will decline over time. The current law benefit outlays for those who delay retirement or who are penalized by the earnings test are drawing closer to the amounts that would be paid out if the earnings test did not exist. That means that the cost of repealing the test will not rise indefinitely over time, but will decline to zero after 2005.

Effect on work effort.

Additional work effort and taxable income due to repeal of the earnings test could result in additional tax revenue equal to about half of the cost of repeal. There would also be some recovery of the cost due to taxation of a portion of the higher benefit payments.

Among the roughly 400,000 people exposed to a range of marginal tax rates between 65 and 85 percent, repeal of the earnings test would reduce their marginal rates to a range of about 15 to 35 percent. This would raise their after tax wage at the margin by about 150 to 300 percent. This is a very large increases in the incentive to work. It would not be surprising, given normal labor supply responses, to see an increase in work effort and earnings on the order of 50 to 100 percent by members of the affected group. Perhaps 200,000 to 300,000 individuals would work significant extra hours.

Some retirees who are not affected "at the margin" by the earnings limitation, such as those who have lost all their benefits to the test, might work less if their benefits are restored. They might use the higher income to buy more leisure. This is called the "income effect". Most researchers make a serious overestimation of the income effect. It is simply not powerful enough to offset the effect of huge increases in the after-tax wage in encouraging additional work effort.

Very conservative estimates by SSA, including a large negative income effect, suggest additional earnings of $0.5 to $1.0 billion per year by retirees age 65 through 69 in the event of repeal, producing additional revenue from taxation of benefits of between $0.1 and $0.2 billion per year, and between $0.1 and $0.2 billion in additional income and payroll tax revenues. Each effect would offset about 5 percent of the cost of repealing the earnings test for this age group. Without the questionable large negative income effect, reflow from taxation of earnings could exceed 50 percent or more of the higher benefits paid.

Estimating behavior and revenues.

It should be noted that any revenue estimates on the tax consequences of eliminating the earnings test prepared by the Joint Tax Committee, the Congressional Budget Office, or Treasury will likely include only the revenue from the direct taxation of the added benefits paid. The estimates will be unlikely to include any revenues due to higher employment and earnings of the elderly as a result of the repeal. Each agency as a matter of policy sticks to an unchanged economic baseline forecast in performing revenue estimates. Real world changes in GNP and associated revenue changes due to a policy shift are ignored.

The rationale behind this "static" estimation technique is three-fold. First, there is no consensus in the economics profession on the precise means by which taxes and transfers affect behavior; while it is known that some policy changes are more likely to alter behavior than others, the absolute and relative magnitudes are not agreed upon. Second, "dynamic" revenue estimation is of course more work. And third, there is concern that, in the absence of precise agreement as to rules of determining behavior changes and revenue reflows, interest groups and bill sponsors might have even more incentive than at present to make exaggerated claims for their favorite legislation.

The one certainty in all this is that the effect of a policy change is not zero. While no revenue reflow estimate will ever be perfect, the assumption of zero reflow is bound to be incorrect, and acts to exaggerate the cost of pro-growth policy changes.

Financing repeal of the earnings test.

Repeal of the earnings test is most often discussed for ages 65 through 69, where complete repeal would cost about $5 billion per year in higher outlays, before offsets. As mentioned above, about half of this cost might be recovered through higher income and payroll taxes due to higher earnings under reasonable assumptions, but these revenue reflows would not be counted under the current budget scoring rules. Another five percent, $0.1 to $0.2 billion, might be recovered automatically from income taxation of the additional benefits paid out. The latter would be counted under budget scoring rules.

Minor adjustments to the benefit computation process. Minor adjustments to the benefit computation process that have been considered at one time or another by SSA and the Congress might be employed to provide additional savings. For example, accelerating the increase in the delayed retirement credit to 8 percent in 1989 would encourage later retirement, and save about $0.4 to $0.5 billion per year. Eliminating the recomputation of benefits for additional earnings after reaching normal retirement age could save about $0.8 billion per year. Elimination of the excess earnings exception and the unreduced auxilliary beneficiary exception to the rule prohibiting retroactive entitlement in reduced benefit cases would save about $0.2 billion per year. Administrative cost savings of nearly $0.1 billion should be counted as well. These steps would cover about one-third the cost of the repeal.

Phasing in the reform. A phase-in of the reform could make the task even easier. Assuming no offsets or tax reflows, eliminating the test for those age 69 in 1990, age 68 in 1991, and so on would cost under $1 billion the first year, rising in stages to the full $5 billion in 1994. During this period, normal real economic growth will be raising real Federal revenues by about $30 billion each year, or by over $150 billion annually by 1994. To implement this reform would take only a bit over 3 percent of the real growth of revenues over five years, even without offsets and measured on a purely static basis.

Accelerating the scheduled increase in the normal retirement age. The 1983 Social Security Amendments provided for an increase from 65 to 67 in the normal retirement age, which is the age at which a retiree may collect full benefits. The age will rise from 65 to 66 at a rate of two months per year for those reaching age 62 between 2000 and 2005; it will rise from 66 to 67 for those reaching age 62 between 2022 and 2027. The provision will still allow retirement at age 62, with an early retirement penalty of 5/12 percent for each of the additional 24 months of early retirement permitted under the change.

Accelerating the current law retirement age increases by ten years, to begin the phased increases in 1990, would save enough in outlays to cover half the cost of repealing the earnings test by 1995. The rise in the retirement age is very gradual. Someone turning age 62 in 1990, and planning to retire at age 65 in 1995, would have to plan on working two additional months in 1995 to collect full benefits. Someone planning on early retirement at age 62 in 1990 could choose between two additional months of work or an additional early retirement penalty of less than one percent of the primary insurance amount.

BUDGET SAVING FROM RAISING NORMAL OASDI RETIREMENT AGE TO 66
IN STAGES (two months per year), 1990-1995
(millions of dollars)

Fiscal Year	Reduced OASDI Outlays	Reduced Outlays plus Increase in Payroll Tax	Reduced Outlays plus Increase in Payroll and Income Tax
1990	51	76	101
1991	162	189	216
1992	489	547	605
1993	1,011	1,072	1,133
1994	1,754	1,851	1,948
1995	2,682	2,785	2,888

Early retirement penalty. Consideration should also be given to eliminating the earnings test for those below normal retirement age. Perhaps the early retirement penalty could be adjusted slightly to defer part of the cost. However, this should not be done without considerable advance notice to give people time to save or to plan to work an additional few months to make up for the change in the benefit computation procedure.

Reducing replacement rates. Finally, some consideration could be given to a small adjustment to the benefit formula itself, effective some years from now. As shown in the attached table, derived from table F-6 in Appendix F of the 1989 Social Security Trustees Report, the current formula provides for very large increases in real benefits per retiree in the years ahead. Perhaps a trade-off could be devised of a reduction in the projected outyear benefit increases and replacement rates (benefits as a percent of pre-retirement earnings) in exchange for a phase-out of the earnings test for the lower age group.

Incidence of the reform.

Much will undoubtedly be made over the distribution across income classes of added benefit payments under repeal of the earnings test. However, while repeal may send additional benefits to upper income persons, they are likely to be taxed on those benefits to a greater degree than others who benefit from repeal. In addition, no one should have to face tax rates of 65 to 85 percent, let alone rates over 100 percent. The latter are virtually federal orders of forced retirement. Even a 65 percent rate violates the spirit of tax reform.

Conclusion

It would be extremely beneficial from an economic, tax simplification, administrative, and personal liberty standpoint to repeal the social security earnings test. Budget and distributional concerns are minor by comparison with the benefits to be had from this reform, and can be dealt with via phased reductions and other adjustments to the benefit computation rules.

ESTIMATED REAL BENEFIT AMOUNTS PAYABLE TO RETIRED WORKERS
UPON RETIREMENT AT NORMAL RETIREMENT AGE*
WITH VARIOUS PRE-RETIREMENT EARNINGS LEVELS
BASED ON ALTERNATIVE II-B ASSUMPTIONS,
CALENDAR YEARS 1989-2065

	CONSTANT 1989 DOLLARS			PERCENT OF EARNINGS		
Calendar year	Low**	Average	Maximum***	Low**	Average	Maximum***
1989	$5,016	$8,022	$10,795	57.5	41.4	24.0
1990	5,031	8,286	11,210	56.9	42.2	24.4
1995	5,212	8,609	11,959	55.8	41.5	24.6
2000	5,547	9,162	13,208	55.8	41.5	25.4
2005	5,852	9,685	14,448	55.3	41.2	26.1
2010	6,228	10,305	15,829	55.3	41.2	26.8
2015	6,631	10,969	17,173	55.3	41.2	27.3
2020	7,053	11,669	18,350	55.3	41.2	27.4
2025	7,455	12,355	19,398	54.9	41.0	27.2
2030	7,933	13,147	20,648	55.0	41.0	27.3
2035	8,441	13,989	21,963	55.0	41.0	27.3
2040	8,982	14,886	23,374	55.0	41.0	27.3
2045	9,559	15,841	24,874	55.0	41.0	27.3
2050	10,171	16,855	26,469	55.0	41.0	27.3
2055	10,823	17,936	28,164	55.0	41.0	27.3
2060	11,517	19,086	29,966	55.0	41.0	27.3
2065	12,255	20,309	31,883	55.0	41.0	27.3

* Normal retirement age at which full benefits are payable is currently 65. This will rise to 66 in stages (two months per year) for those reaching age 62 between 2000 and 2005, and to 67 in stages for those reaching age 62 between 2022 and 2027.

** Earnings equal to 45 percent of average.

*** Earnings equal to the SSA contribution and benefit base (maximum covered earnings).

Chairman **Jacobs**. Mr. Smedley.

STATEMENT OF LAWRENCE T. SMEDLEY, EXECUTIVE DIRECTOR, NATIONAL COUNCIL OF SENIOR CITIZENS

Mr. **Smedley**. Thank you, Mr. Chairman. In the interests of time, I will summarize my summary orally.

Chairman **Jacobs**. That is very good.

Mr. **Smedley**. First, the National Council of Senior Citizens believes that if you examine the retirement test objectively, how it works and who benefits by its liberalization and what the cost impact of its liberalization will be—if you do that objectively, there are some obvious conclusions.

The retirement test measures whether a person has retired. If the contingency insured against does not take place, you don't get paid for it. You don't get your fire insurance unless you have a fire. You don't get your auto insurance unless you have an auto accident.

I can't add much to the CBO and Social Security Administration statistics. They have published studies and explained them in testimony today. But it is clear from all of the data that the ones that benefit from the liberalization or elimination of the retirement test are the higher income elderly.

In the time of a budget crisis and deficits, this is not the best use of Federal funds.

Much has been made of labor force participation today, but if you examine the past when liberalizations of the retirement tests have taken place, there has been no significant impact on labor force participation.

If you examine the national retirement system of foreign countries that use the annuity approach and do not have retirement tests, those industrial countries do not have any better labor force participation than we do. In many cases, it is less.

And finally, Mr. Chairman, a major liberalization will take place in the retirement test next year. The penalty after the exempt amount will be reduced to $1 for every $3 of earnings. The delayed retirement credit will be gradually phased in from 3 to 8 percent.

It seems to us it makes no sense to liberalize further, even before liberalization in present law goes into effect.

In short, Mr. Chairman, after careful consideration, the National Council of Senior Citizens has concluded that further liberalization of the retirement test at this time is not warranted.

Thank you.

Chairman **Jacobs**. Thank you, Mr. Smedley, for your testimony.

[The statement of Mr. Smedley follows:]

Executive Director
Lawrence T. Smedley
Washington, DC

National Council
of Senior Citizens

Jacob Clayman
Silver Spring, MD

Statement by

Lawrence T. Smedley
Executive Director

Good morning Chairman Jacobs, members of the Ways and Means Subcommittee on Social Security. I am Lawrence T. Smedley, Executive Director of the National Council of Senior Citizens. The National Council of Senior Citizens appreciates this opportunity to address the issue of the Social Security retirement test. There has been considerable interest recently as to whether the retirement test should be eliminated. In evaluating this issue, we believe it is important to consider why the test exists and how it works, who it affects, the distributional impact and cost of its repeal and an assessment of other options that may exist. We commend Chairman Jacobs for holding today's hearing. After careful consideration, the National Council of Senior Citizens has concluded that modification of the Social Security retirement test is not warranted at this time, particularly in light of the significant liberalization which will occur next year.

Why is There a Retirement Test and How Does it Work?

Social Security retirement benefits were designed to protect workers against the loss of income in old age due to retirement. For this reason, the retirement test was designed to determine whether or not a worker was substantially retired and thus entitled to benefits. To have made Social Security an annuity program permitting the payment of benefits to people with unlimited earnings after retirement would have required much higher contributions from workers, employers and the self-employed than they have been paying all these years.

The original concept of the retirement test has been modified many times, gradually allowing retirees to earn greater amounts of income without losing their Social Security benefit. Under present law, an older worker can earn up to a specified income level with no loss of Social Security benefits. Currently, this level is $6,480 for workers 62 to 64; $8,880 for workers 65 to 69. Earnings in excess of these amounts reduce the beneficiaries' Social Security payment by $1 for every $2 of earned income ($1.00 for every $3.00 starting next year). This means a worker age 65 to 69, with an average Social Security payment of $500 a month, would not lose all benefits until he or she earned $20,400. The earnings levels are indexed automatically every year. Once a worker attains the age of 70, he or she may earn unlimited income with no loss of Social Security benefits.

Who is Affected by the Earnings Test?

According to a 1988 CBO analysis, "fewer than one in ten people aged 65 through 69 who are eligible for Social Security benefits is affected by the earnings test, and the characteristics of those affected are quite different from those of the average beneficiary." They determined that, "while only about one-eighth of all beneficiaries had family incomes in 1986 above $42,000, more than 40 percent of those affected by the earnings test had incomes above that level. In contrast, nearly 40 percent of all beneficiaries had incomes below $15,000, compared with only five percent of people with earnings above the exempt limit."

The study looked at the approximately 600,000 persons aged 65 to 69 who received lower benefits because of the earnings test. The CBO profile found these persons more likely to be male, to live with their spouses, to have family incomes above $32,000, and to have family incomes above four times the poverty threshold (about $21,000 for a single person and about $26,500 for a couple). Significantly, while roughly one-third of comparable Social Security recipients had incomes below 200 percent of the poverty line (about $10,500 for single persons; $13,300 for couples), only one percent of those affected by the earnings test had incomes at such levels.

The CBO numbers are comparable to the 1987 House Republican Research Committee Report, based on data from the Social Security Administration. They determined that beneficiary families for whom repeal of the earnings test would have no impact had median income of $14,700; those who would receive additional benefits had median incomes of $27,700; and those who currently lose their entire benefit (and would, therefore, gain the most from repeal of the test) had median income of $37,700.

According to the "Social Security Bulletin,"[1/] workers with higher earnings before entitlement to Social Security benefits have higher earnings after entitlement and are also more likely to continue to work. Consequently, NCSC has long been concerned that repeal of the earnings test would provide a windfall benefit to a small percentage of older persons with, presumably, the least need for additional income and the greatest ability to increase their income through work. This concern is sustained by the CBO analysis. The report, in examining the impact of modifying and eliminating the earnings test, found that, while small increases in the earnings limit primarily benefit comparatively lower-income families, larger increases or repeal primarily benefit higher-income families.

For example, the CBO reports that about half of affected people in families with annual incomes below $15,000 would not have had their benefits reduced if the earnings limit had been $9,000 in 1986. That level would have exempted just five percent of affected people with family incomes above $42,000. Measuring the income of affected households relative to the poverty threshold, CBO found that doubling of the earnings test in 1986 would have exempted virtually all people with family incomes below 300 percent of poverty, while leaving about two-thirds of those with incomes above four times the poverty level subject to benefit reductions.

Even so, the CBO points out that, even under the smallest increase in the earnings limit, only a small fraction of those made exempt would have low incomes. Less than half would be in families with incomes below $25,000--a level which is still considerably higher than median income of all elderly households. Only a quarter of all elderly households have income exceeding $25,000 annually. Raising the earnings limit at the lower end would, however, disproportionately benefit persons who are widowed or were never married, particularly women.

Would Repeal of the Earning Test Encourage Continued Employment of Older Persons?

The most common reason given for repeal of the earnings test is that it is a disincentive to the continued employment of older workers. Proponents argue that the test represents a prohibitive tax on earnings at the margin, causing workers to deliberately hold down their work level to avoid loss of benefits or seek to be paid "under the table," allowing them to avoid reporting their full earnings. But a study by the Congressional Research Service, released earlier last year, concluded that there is simply little or no data about these behavioral assumptions.

Furthermore, for low-wage earners, the earnings test is no disincentive because they are unable to earn up to the allowable level. A person working full time, year-round, at the current minimum wage of $3.35 an hour, would earn just $6,700--well below the earnings threshold. Many older workers prefer part-time employment. A person could earn 2-1/2 times the minimum wage, working 20 hours a week, year-round, and still not exceed the threshold.

It is also relevant to note that, while many older persons need and want to continue working, the trend in this country has been toward earlier retirement. According to an analysis in the "Social Security Bulletin," retirement as late as age 65 is becoming somewhat unusual. For many, particularly those with

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[1/] November 1987. Vol. 50 No. 11.

adequate incomes, early retirement is voluntary. For others, health limitations, market forces, or physically demanding occupations which become more difficult to maintain with advancing age compel retirement.

Elimination of the earnings test will not bring jobs to depressed areas or retrain displaced workers for new jobs. It will not end a still-pervasive bias by many employers against hiring and promoting older workers. And, unfortunately, too many older workers continue to find themselves coerced into early retirement.

Better enforcement of age discrimination laws, more adequate job training or retraining for older workers and more funding for the Senior Community Service Employment Program, Title V of the Older Americans Act, would do much more to encourage the continued employment of older workers.

The Title V program provides part-time community service jobs for low-income older workers. These minimum-wage jobs provide vital opportunities for about 65,000 older persons of limited incomes who, without such assistance, would often not have the skills or opportunities to find employment on their own. Current Federal spending on this necessary and effective program amounts to just $344 million a year. Many more low-income older persons could benefit from this program, if additional revenues were allocated for its expansion. Additionally, it seems particularly misguided to us for the Committee to act on this matter, while under another program within the jurisdiction of the Ways and Means Committee--Supplemental Security Income (SSI)--inadequate benefits are being provided and insufficient outreach is being done to potential beneficiaries.

All that aside, as a result of 1983 amendments to the Social Security Act, changes to the earnings test are already scheduled to take place. Starting next year, workers will have their benefit reduced one dollar for every three dollars of earnings over the exempt level. In addition, liberalization of a work incentive called the "delayed retirement credit" has already been enacted. At present, workers who delay their retirement beyond the "normal" retirement age (currently age 65) receive a three percent annual increase in their Social Security benefit once they retire. Between 1990 and 2009, this credit will gradually increase to eight percent. This is the level that has been actuarially determined to fully compensate workers for lost benefits once they retire.

Fiscal and Political Ramifications of Repeal

If the retirement test was raised by $3,000 each year from 1990 to 1993 and eliminated entirely in 1995, as some have proposed, the five-year cost would be $6.3 billion. Even raising the limit only $1,000 would cost about $240 million annually. Outright repeal would cost $24 billion over a five-year period.

In an era of budget constraints, spending $24 billion to give higher Social Security benefits to a very small number of persons with higher than average incomes is not justifiable. It is unlikely that repeal would bring new workers into the labor force, although it might increase the work effort of a small group of workers. Even so, next year, the test will be significantly liberalized, allowing greater earnings retention by older workers. While NCSC would not be opposed to revisiting the consideration of a small increase in the retirement test at some point after the impact of next year's provisions are analyzed, further modification of the test now would be, in our view, costly and ill-advised. We urge members of Congress who seek to promote greater work effort by older persons to seek other alternatives.

Chairman JACOBS. Mr. Entin, in your closing remarks you asserted that the highest income people had higher marginal tax rates. You didn't say that?

Mr. ENTIN. Given the thresholds of the taxation of benefits, I say that if the benefits increase, the people who would be subject to the tax on the additional benefits would be over the threshold. The very highest income people——

Chairman JACOBS. So you weren't talking about income tax rates. You are aware that the highest income people of the United States have a lower marginal rate than people who make less than they do, under the wisdom of the 1986 act?

Mr. ENTIN. Yes; I agree with you there. I did not say they had a higher rate.

Chairman JACOBS. Good, OK. Thanks very much to the panel.

Our final panel today consists of a representative for the National Federation of the Blind, James Gashel, and a representative for the National Committee to Preserve Social Security and Medicare, William J. Lessard.

Mr. Gashel.

STATEMENT OF JAMES GASHEL, DIRECTOR OF GOVERNMENTAL AFFAIRS, NATIONAL FEDERATION OF THE BLIND

Mr. GASHEL. Thank you, Mr. Chairman. By virtue of a Social Security amendment in 1977, section 223(d)(4) of the Social Security Act links the earnings cap applicable to blind disabled workers to the exempt amount applicable to persons who are retirees age 65 through 69. That link would be broken unwisely, we think, by section 2(c) of H.R. 2348.

There is another bill also pending before this subcommittee, which is H.R. 8. It has got a lot of cosponsors in the House. We think it is even more unwise, since it would set the earnings cap for blind individuals at $85, rather than the current $740 a month, and we definitely can calculate the difference. So both of those proposals, we would oppose.

We do support, however, maintaining the linkage between the earnings limitation for blind persons of any age and people who retire at age 65. Some understanding of the characteristics of the blind population as a whole helps to give you the rationale for that position.

Consider the blind person age 70 or older. Those people who are able to work have the maximum incentive to do so. There is absolutely no limitation on their earnings. Then for the blind individual who has attained age 65 but is not yet 70, there is still some incentive to work by virtue of the one-for-two earnings setoff, which will become one for three.

At least benefits are not withdrawn abruptly for individuals aged 65 through 69. Even that earnings incentive or work incentive, the setoff which I mentioned, is withdrawn altogether in the case of the blind person who is of working age. This is the larger group of blind individuals.

In my written statement, Mr. Chairman, I have explained the basis for the linkage between the group of blind beneficiaries and retirees. As with retirees, blindness is a defined condition in the Social Security Act.

Of the 498,000 blind people in the United States who are blind under *the definition in the act*, 54 percent have attained at least age 65. With few exceptions, they are currently beneficiaries.

Now, if you add to that picture the working-age blind who are currently beneficiaries to the 54 percent, that number now becomes 82 percent. Most blind people of any age simply do not work and already receive Social Security benefits. Eight percent of the remaining blind persons not included in these numbers are individuals who are under age 18. We conclude that less than 10 percent of the blind population is working to the extent that they do not currently qualify for Social Security benefits.

We know that there are certain social and economic consequences which almost always accompany blindness. Being outside of the work force is almost always the major factor. Maintaining an earnings limitation in the case of blind persons or retirees mixes a welfare or a means test approach with an insurance program.

In Social Security terms, Social Security is insurance, not welfare. Its benefits are payable to the rich, even the very rich, and they are also payable to the poor. Wealth, or the lack thereof, has absolutely no bearing on a person's ability to collect Social Security benefits. Only work activity penalizes a person in terms of his or her receipt of benefits.

This is done not to limit income, as I have said and has been said many times, but it is simply done to limit the amount of work one does. In our opinion, for blind people that is an absolutely wrong approach.

In the economic terms of Social Security, removing the earnings limitation now applied to all blind people would increase the beneficiary roles by only a very minuscule fraction, adding approximately 30,000 to 40,000 individuals to the rolls.

The payoff for the Social Security System in economic terms would be the newly generated revenues resulting from the maximum work incentive that would be given to approximately 130,000 blind beneficiaries and their dependents of all ages. These are people who, in many instances, may well be capable of working. For the most part, these, however, are individuals who now draw benefits and do not work.

Mr. Chairman, thank you for the opportunity to appear once again before this subcommittee on the matter of the earnings limitation and its effect on the legally blind population.

Chairman **Jacobs**. Thank you, Mr. Gashel.

[The statement of Mr. Gashel follows:]

BEFORE THE SUBCOMMITTEE ON SOCIAL SECURITY

COMMITTEE ON WAYS AND MEANS

UNITED STATES HOUSE OF REPRESENTATIVES

WASHINGTON, D.C.

STATEMENT OF THE

NATIONAL FEDERATION OF THE BLIND

JAMES GASHEL

DIRECTOR OF GOVERNMENTAL AFFAIRS

MAY 25, 1989

Mr. Chairman, I am James Gashel. I am Director of Governmental Affairs for the National Federation of the Blind (NFB). My address is 1800 Johnson Street, Baltimore, Maryland 21230. Thank you for offering me this opportunity to present the views of the NFB in response to the Social Security Subcommittee's interest in reviewing options for modifying the retirement test.

There are over fifty thousand blind people who are members of the National Federation of the Blind. We have a local chapter of the Federation in almost every sizable population area in this country and a state affiliate in all states and the District of Columbia. In short, Mr. Chairman, NFB is organized and active in all parts of the United States.

By virtue of its size and scope NFB represents and speaks for the blind as a collective body. We speak for older blind persons and younger blind persons as well. The positions we express in hearings such as these are the result of the democratic process of debate and decision-making. The supreme authority of the Federation is its National Convention, which occurs annually. During the convention we openly debate (and approve or disapprove) a number of policy resolutions. In this manner the Federation is truly the blind speaking for themselves. It is not simply an organization speaking for the blind. All of our elected officers and the vast majority of our members are blind. For these reasons the NFB is widely known as the voice of the nation's blind.

This hearing concerns the Social Security retirement test and various approaches that may be taken to modify it. Blind people have a special concern in relationship to this subject. Most blind people are age 65 or older. The National Society to Prevent Blindness has estimated that there are 265,950 blind retirees (age 65 or older) in this country. According to the same data there are 498,000 blind persons (of all ages) who meet the Social Security Act's definition of blindness.

The retirement test affects blind retirees in much the same way that it affects all senior citizens aged 65 through 69. But the retirement test also affects blind people under age 65 who receive Social Security benefits. This latter group is made up of about 85,000 blind "disabled worker" beneficiaries. Under a provision in section 223(d)(4) of the Social Security Act, these individuals are subject to a test of "substantial gainful activity" which exempts average monthly earnings that do not exceed the "exempt amount" for Social Security retirees under section 203(f)(8) of the Act. The amount of allowed earnings under this section is currently $740.00 per month, subject to upward adjustment in January, 1990, and at the beginning of each succeeding calendar year. Unlike other individuals described in section 203(f)(8), blind individuals who have not attained age 65 are not subject to the "excess earnings" principles of section 203(f)(3). So for these individuals the "exempt amount" of $740.00 is an absolute earnings cap.

Blind beneficiaries of all ages (not just the retirees) are likely to be affected by any changes that Congress may make in the retirement test. Certainly the majority of blind individuals would be affected as retirees. Those who are not yet retirees, but are subject to the same basic "exempt amount," would also be affected in some way if Congress decides to raise the retirement age or to eliminate the retirement test altogether.

Keeping this background in mind, it is our considered position that Congress should maintain the rationale of a linkage between blindness, as a defined disability, and attainment of age 65, as the legally defined age of retirement. When an individual becomes blind as defined in the Social Security Act, a continuous "period of disability" is established. However, this status as continuously disabled does not carry with it continuous entitlement to cash benefits. A blind person's entitlement to cash benefits ceases when earnings reach the average monthly earnings cap of $740.00. Thus the present posture of the law tends to align the treatment of earnings of blind beneficiaries (under age 65) with the treatment of earnings of retirees (blind or not) aged 65 through 69. This alignment is appropriate and should continue if the retirement test is modified.

Mr. Archer's bill, entitled the "Worker's Option Act of 1989" (H.R. 2348), proposes elimination of the Social Security retirement test altogether for persons who have attained age 65 beginning in 1990. The amendment made by section 2(c) of the bill would continue an earnings cap in the case of blind beneficiaries under section 223(d)(4) of the Act. This provision of the bill departs from the statutory relationship between blindness and retirement age, which Congress forged in 1977. As I have already said, we believe that the current statutory linkage between the exempt amounts for blind persons and retirees is rational and should be maintained. It is also our position, Mr. Chairman, that in either case (blindness or retirement) there should not be a cap on earnings.

In contrast to Mr. Archer's bill, Congressman Steve Bartlett has introduced the "Social Security Work Incentives Act" (H.R. 8), concerning the treatment of earnings of disabled worker beneficiaries under title II of the Social Security Act. Ironically, H.R. 8, with a drastically curtailed earnings cap in the case of blind beneficiaries, purports to encourage the disabled to work. It is beyond comprehension, Mr. Chairman, to think that Congress may enact legislation to eliminate the earnings limitation for retirees--the largest group of beneficiaries under Social Security--while drastically cutting the exempt earnings amount for the blind--one of Social Security's smallest beneficiary groups.

Treating the blind as "disabled" by using some form of a SGA test is inappropriate and unnecessary. Blindness is a defined and detectable physical condition with predictable economic and social consequences that flow from it. Blindness is, in fact, the only physical impairment that is actually defined in the Social Security Act. Identification of blindness in conformity with this definition can be made quite reliably by an ophthalmological examination.

For the disabled who are not blind, SGA is generally a measurement tool that is used to define disabilities. Thus, in Social Security terminology, a person is "not disabled" if he or she has demonstrated an ability to engage in (or is actually engaging in) SGA. On the other hand, the person is "determined to be under a disability" if he or she cannot perform SGA. In blindness cases, however, SGA measurements tell us nothing about the existence (or absence) of disability. The disability in these cases is determined by applying the definition in the Act. The only effect of the SGA measurement in SSDI blindness cases is to limit work activity of blind persons. That in our view is a totally counterproductive use of the SGA concept.

In SSI blindness cases, on the other hand, SGA is not applied. Income of blind persons eligible for SSI is, of course, limited by income restrictions of SSI unrelated to the definition of disability. But a measurement of "Substantial Gainful Activity" in blind SSI cases is not a factor whatsoever. That is an entirely appropriate way to handle the determination of blindness. The fact is, that as the Social Security Act accurately recognizes, blindness exists as a particular physical condition regardless of SGA.

If some form of a SGA test should not be applied to the blind, how should earnings of the blind be treated? This question brings me back to the matter of the retirement test. Social Security is not a means tested program, aimed at only the poor and not the wealthy. This is as it should be. Earnings, however, are limited, but they should not be. Here is the rationale for this position.

Blindness as we still experience it today has profoundly adverse social and economic consequences. Therefore, Social Security benefits should offset these consequences insofar as possible. The social attitudes about blindness are full of myths and misconceptions. As a group, the blind face an incredibly devastating set of artificial impediments when they seek to enter and compete in the labor force. The blind are not just viewed as unemployed. We are usually considered unemployable.

To be sure, the blind pay a heavy price for this erroneous labeling. For example, most people agree that over seventy percent of the employable blind population is either unemployed or underemployed. If before blindness an individual had an income of, say, fifteen thousand dollars annually (not an uncommon income for sighted individuals), and if after blindness that same individual finds employment at $8,500.00 annually (not at all an uncommon experience for the blind), he or she will still not be eligible to continue receiving full Social Security benefits despite the fact that a substantial loss of income has occurred. Blind individuals who have not attained age 65 would not be entitled to benefits at all in the circumstances just described.

Under the present conditions prevailing in our society the blind are required to suffer the indignity of being cast aside in competition for jobs and social opportunities, and we are also required to pay in terms of cold cash for our second-class status. The social attitudes about blindness which have traditionally prevented us from assuming the more responsible positions and holding the more lucrative jobs in the labor force have been fostered by society as a whole, not just by the blind members of society. In fact, these attitudes have not principally been fostered by the blind at all. Therefore it is equitable for us to propose that everyone should share in carrying the financial burden imposed on us by these social attitudes--a burden which we now bear alone.

Another set of economic consequences facing the blind is the result of the Social Security system itself. I refer here to the disincentive factor which inhibits the initiative of any blind person who is naturally concerned about some degree of long-range economic security. The economic realities are these: under existing law, if an individual becomes blind and has average monthly earnings which do not exceed the "exempt amount," he or she will likely draw full Social Security benefits. The individual has every incentive to remain unemployed and not return to work at all. Why? In the first place, he or she is probably not an expert in the law. The law is complex, and the talk of allowed earnings, trial work periods, and the like is confusing and not generally conducive to an attempt to resume or continue working.

The penalties for working are even greater for blind individuals who have not yet attained age 65. If the individual goes to work and (after a specified trial work period) is earning somewhere in the neighborhood of $740.00 per month, benefits will be terminated abruptly. Ironically, earnings of a blind individual have a much less dramatic effect on benefits upon attainment of age 65 and no effect whatsoever when the individual reaches age 69. Blind persons under age 65 with dependents may in some instances receive over $1,500.00 per month, the current family maximum. All of this will be lost when earnings exceed 740.00 per month. The individual with very modest earnings of $800.00 or $900.00 per month, for example, is penalized for having tried to become self-supporting.

Place yourself in the position of a blind person considering possible employment. Remember that, including dependents' benefits, the family income from Social Security may exceed $1,500.00 per month. I know a number of blind people who (believing in the work ethic) would accept employment offering gross wages at somewhat less than their possible Social Security income. They must, however, also consider deductions for income and Social Security taxes, as well as a variety of expenses related to their work. Commonly a blind person finds it necessary to employ a reader or driver, and these expenses lower the take-home pay even more. Facing such circumstances, can a blind person afford to take a job at the risk of economic security? Some think they can, but many have found that they simply cannot.

Retirees and blind individuals of all ages should become entitled to Social Security benefits after performing a certain amount of covered work. The basis upon which this should be adopted is the broader social benefit which would result if an entire segment of the population whose talents are now underutilized were to be made fully productive. Under this proposal the blind beneficiary of any age would know that he or she could count on a monthly insurance payment. It would not be jeopardized by attempted work. The blind person is better off (and society generally is better off) for the person to be productive instead of idle--working instead of sitting at home.

Proposals to eliminate the earnings limitation have traditionally misapplied a welfare concept to Social Security, which is not welfare. For example, proponents of the earnings limitation complained that individuals with high earnings would continue to receive their Social Security benefits. But the fact is that the number of blind people being paid say $30,000 or more annually is very small. Most blind people do not even work.

Especially in the case of the blind, consider how the work incentives in Social Security are really out of focus with the work capability of blind people. More than half of the blind population is aged 65 or older. Many have worked enough (especially as sighted people) to be qualified for Social Security retirement benefits. These older blind people (who are mostly outside of the workforce) have a greater work incentive than do the blind who are between the ages of 18 and 65. This is because of the treatment of excess earnings under section 203 (f)(3).

Once a blind person reaches age 70 (as in the case of all retirees), the work incentive actually increases. At that time the limitation on earnings is removed altogether. This means that the few blind people who can still work at age 70 or older can earn to their heart's content even if they are earning over $30,000. Meanwhile, their blind counterparts aged 64 and below are limited to earning no more than $740.00 per month. Many of these people could actually work more (subject to job availability) if they had the same work incentive as their blind counterparts at age 70 or older. But the fact is that these younger blind people are actually being paid to stay outside of the workforce. This approach is wrong.

Removing the earnings limitation could add an estimated 30,000 to 40,000 blind individuals to the beneficiary rolls. The payoff (from the income side of the Social Security system) is the maximum work incentive that will be aimed at the blind of all ages who now receive any type of Social Security benefit. Fewer blind individuals would receive SSI as a result of becoming Social Security beneficiaries. There would actually be a positive cost impact on the Social Security system resulting from increased payments into the trust funds by those who are now beneficiaries. The greater their earnings, the greater will be the amount that they pay into the trust funds. We estimate, conservatively, that as many as 130,000 blind beneficiaries of all ages and their dependents will receive an added work incentive by the earnings limitation removal. Then the benefits they receive will be offset in part by the taxes they will pay. Now they only receive benefits and do not pay Social Security taxes in most instances.

Mr. Chairman, in concluding this testimony, I would like to restate and reemphasize the message that we have been giving to this subcommittee and the Congress for several years. The blind as a group are prepared to work and work hard. The legislation which we recommend to your attention constitutes an effort on our part to renounce our traditionally established lives of demeaning dependency and subordinate status. In asking for work incentive legislation we express our firm determination to escape from many long decades of custodialism during which we have been constrained by society's ignorance, myths, and misconceptions. We seek to free ourselves from the captivity of ignorance, prejudice, and discrimination. We ask only the opportunity to lead normal, self-supporting, independent lives. For our part, Mr. Chairman, we are committed to use work incentives effectively as instruments of rehabilitation, self-help, and self-support for the blind. On behalf of the National Federation of the Blind, I thank you.

Chairman JACOBS. Mr. Lessard.

STATEMENT OF WILLIAM J. LESSARD, JR., DIRECTOR OF POLICY AND RESEARCH, NATIONAL COMMITTEE TO PRESERVE SOCIAL SECURITY AND MEDICARE

Mr. LESSARD. Mr. Chairman, our members are encouraged by the impetus given to liberalizing the retirement test by recent legislative action, and we hope that this hearing will lead to House action.

I also want to emphasize our support for actuarially fair benefit adjustments for all workers who delay retirement. I have attached to my testimony the national committee's position paper entitled "Working Widow Equity Proposals."

Since short-term cost is one of the concerns of the subcommittee, we would recommend phasing in the retirement test elimination, actuarially fair benefit adjustments for all those who delay retirement, and a public education program along the lines suggested by Mr. Myers. This would be in addition to the elimination of retroactive benefits which was recently proposed.

When it comes to retirement, older workers frequently face a catch 22, and we have an example from Mrs. Alexander, a widow in Davis, CA. This example responds to some of the suggestions that Congressman Brown was making regarding possibly offsetting liberalization for those over age 65 with deliberalization for those under age 65.

She is a widow and she took early Social Security at age 62, so I would like to use that example. She writes:

> I was desperate. I could not find work, so I finally gave in and took my husband's Social Security. I was told to work when I could, as I would be given work credit at age 65. Last year, I earned $10,000. Most of my work is from temp agency work. Approximately $2,000 will have to be paid back, which, for several months, will leave me without income completely. When I do work, I am not able to earn enough to live on that income alone.
>
> Am I really coming out ahead? Will these earnings make a difference at age 65? Would I be better off just trying to earn the amount allowed me? And if one continues to work, will additional credits be added when they reach age 70?

Well, these are some of the answers to her questions. First, her immediate income needs are such that she felt she had to apply for benefits and work at the same time. As a result, she had to run very hard to get only a little ahead. Mrs. Alexander is in a poverty trap, and I don't believe anyone would say she had much of an option. On top of that, there is the administrative burden for Social Security in monitoring compliance and the practically inevitable overpayment hardship.

At age 65, she does receive an actuarial adjustment that is fair, but if she continues to work, either because she still has income needs or because she enjoys working, she will permanently lose lifetime Social Security benefits.

The retired worker who works past age 65 currently receives an actuarial adjustment that is only one-third of what would be actuarially fair. But as a widow, Mrs. Alexander's loss would be even greater because her widow benefits are capped at the age 65 benefit of her deceased spouse. Is it any wonder most workers leave the work force at age 65 if they have not retired earlier?

As a practical matter, the subcommittee must concern itself with the costs before it will act on proposals to eliminate or liberalize the retirement test. The national committee, in principle, would disregard constraints of the budget referred to in the subcommittee's press release because we agree with you and 66 other Members of the House who have cosponsored H.R. 933 that would take Social Security completely out of the budget and Gramm-Rudman-Hollings.

Nevertheless, we recently supported a legislative proposal to finance the short-term cost of liberalizing the retirement test by eliminating retroactive benefits. For the most part, this would not cause undue hardship or even a loss in lifetime benefits.

Since the long-term cost is negligible, the major cost issue boils down to timing, the short-term costs, and even the short-term costs may be overblown due to static analysis. But we believe the short-term costs can be further managed by phasing in an increase, implementing equitable delay retirement credits, and starting a public education campaign.

In addition to the savings, other benefits would flow. Raising the limit would target benefits to low and middle-income workers. In fact, the retirement test has a disproportionate impact on beneficiaries with lower benefits.

Previously, CBO concluded that doubling the earnings limit would exempt nearly half of all affected beneficiaries from the retirement test, completely exempting most women, widows and widowers, and people with low family incomes, and we think that would be a good outcome.

If equitable delayed retirement credits for all retirees were already in effect, there would be complete freedom of choice in terms of what would be to their best economic advantage.

I think in that regard, we would disagree with former Commissioner Ball, who suggested that this is not an area where beneficiaries ought to be given choice. But it would only be effective if they are given an informed choice, and that is where the public education campaign would come in.

We do not recommend that all eligible individuals apply for Social Security benefits at the first opportunity, and we believe that workers and retirees can make their own judgments.

Unfortunately, most individuals receive their first detailed information about actuarial reductions when they go to their Social Security office and have psychologically made the decision to retire. So, frequently, the claims representative does not even discuss delayed retirement credits because they would be working against the psychological barrier.

One component of the education campaign, we believe, should be the perfection and widespread dissemination of the new personal earnings and benefit estimate statements.

Chairman **Jacobs**. We are getting short on time, Mr. Lessard.

Mr. **Lessard**. That is the end.

[The statement of Mr. Lessard follows:]

STATEMENT OF WILLIAM J. LESSARD, JR., DIRECTOR OF POLICY AND RESEARCH, NATIONAL COMMITTEE TO PRESERVE SOCIAL SECURITY AND MEDICARE

Mr. Chairman, I am William J. Lessard, Jr., Director of Policy and Research for the National Committee to Preserve Social Security and Medicare. After testifying last September in favor of eliminating the retirement test, I received several letters of appreciation from National Committee members. Our members now are encouraged by the impetus given to at least liberalizing the retirement test by recent legislative action. We hope that this hearing will lead to House action to liberalize the retirement test.

As I did last year, I also want to emphasize our support for actuarially fair delayed retirement credits (DRCs) for all workers who remain in the work force after full retirement age and urge extension of DRCs to spouses and working widows. I have attached to my testimony the National Committee's position paper entitled *Working Widow Equity Proposals*. Actuarially fair delayed retirement credits and a public education program would help to discourage premature retirement.

When it comes to retirement, older workers frequently face ~~a~~ Catch 22. What do I mean by this? Let's take the example of Barbara Alexander. Mrs. Alexander is a widow living in Davis, California. We received her letter just last week. She writes

> At age 62, I took early Social Security. I was desperate. I could not find work, so finally gave in and took my husband's Social Security. I was told to work when I could as I would be given work credit at age 65. Last year I earned $10,000. Most of my work is from Temp agency work. Approximately $2,000 will have to be paid back, which for several months will leave me without income completely. When I do work, I am not able to earn enough to live on that income alone. Am I really coming out ahead? Will these earnings make a difference at age 65? Would I be better off just trying to earn the amount allowed me? If one continues to work, will additional credits be added when they reach age 70?

Let's examine her situation and consider how frustrated you would be in justifying current Social Security policy to her.

Her immediate income needs are such that she felt she had to apply for benefits and work at the same time. As a result of the Social Security retirement test she has to run very hard to get a little ahead. Mrs. Alexander is in a poverty trap. I don't believe anyone would say Mrs. Alexander had much of an option. Widows and low-earning seniors, in particular, often need both their Social Security benefits and maximum earnings to improve their economic situation. And the low earnings limitation totally drives out of the work force middle-income seniors who are no longer willing or able to work full-time, but would choose to work part-time, if they did not have to forfeit Social Security benefits to do so.

On top of that there is the administrative burden for Social Security in monitoring compliance and the practically inevitable overpayment hardship, which we emphasized in last year's testimony.

The $2,000 Mrs. Alexander loses is roughly the cost of her health insurance which she purchases as part of the group plan of her former employer. Unfortunately, she will lose eligibility to participate in this plan three months before she is eligible for Medicare.

At age 65, Mrs. Alexander will receive an actuarial adjustment that is fair. But if she continues to work either because she still has income needs or because she enjoys working, she will permanently lose lifetime Social Security benefits. The retired worker who works past age 65 receives an actuarial adjustment that is only one-third of what would be actuarial fair. As a widow, Mrs. Alexander's loss will be even greater than that of a retired worker. Her widow benefits are capped at the age 65 benefit of her deceased spouse. Is it any wonder most workers leave the work force at 65 if they have not retired earlier?

As a practical matter, this Subcommittee, however, must concern itself with the cost before it will act on our proposal to eliminate or liberalize the retirement test. The National Committee in principle would disregard "constraints of the budget" referred to in the Subcommittee's press release because we agree with you and the 66 other Members of the House who have sponsored legislation that would take Social Security completely out of the budget and Gramm-Rudman-Hollings. Nevertheless, we recently supported financing the short-term cost of liberalizing the retirement test by eliminating retroactive retirement benefits to retirees and their dependents. For the most part this would not cause undue hardship or even a loss in lifetime benefits.

The long-term cost of eliminating the retirement test to the Social Security Trust Fund is negligible because Congress has already scheduled gradual increases in the delayed retirement credit which would make them actuarially fair in twenty years. Beneficiaries will no longer lose lifetime benefits and Social Security would not save any money as a result of a retirement test. There would even be small savings in administrative costs because the Social Security Administration would be relieved of the administrative burdens of first explaining the earnings limitation, then monitoring post-retirement earnings, and collecting overpayments.

The major cost issue boils down to timing -- the short-term cost. And even the short-term cost may be overblown. Aldona Robbins estimates that "the increase in social security and income tax revenue (from the increased work effort) could offset between one-third and two-thirds of the higher social security benefit outlays." The short-term cost can be further managed by (1) phasing-in an increase in the earnings limit, (2) implementing equitable delayed retirement credits immediately for all individuals and (3) starting a public education campaign so that retirees will have the information needed to make their own choice.

PHASE-IN

First, the earnings limitation could be eliminated gradually as recommended by Congressman Archer. His legislation would lower the age for exemption from the earnings limitation from 70 to 65 one year at a time. Alternatively, the earnings limitation could be gradually removed by incremental increases in the dollar limits for all retirees as suggested by Congressman Wyden and others. Congressman Archer has new legislation similar to Congressman Wyden's except that it applies only to those age 65 and over.

Raising the limit would target benefits to low and middle income workers. In fact, the retirement test has a disproportionate impact on beneficiaries with lower benefits. This year, every beneficiary under age 65 who works full-time at the current minimum wage will lose $244 in Social Security benefits. Because of the higher earnings limitation, 65 to 69 year-old individuals can escape a benefit offset while earning $4.26 an hour full time. The proposed new minimum wage of $4.55 per hour means an older widow or retiree this year would lose $292 in benefits.

DELAYED RETIREMENT CREDITS

Second, by moving forward the scheduled increase in delayed retirement credits and by the addition of delayed retirement credits to spouse benefits, workers could be encouraged to defer receiving benefits which would result in short-term savings.

Higher income older workers under current law presumably would benefit most from removal of the earnings limitation. Yet they would be least likely to apply for Social Security benefits if delayed retirement credits were equitable. The promise of higher future benefits combined with the obligation of paying Federal income tax on half of their Social Security benefits -- and a Catastrophic Medicare surtax on top of that -- is a strong safeguard against a premature rush to apply for benefits.

If equitable delayed retirement credits for all retirees were already in effect, retirees could move in and out of the work force as their own energy, interest, and needs dictated and the economy would prosper from the increased productivity of older workers.

EDUCATION

Third, the Social Security Administration, in cooperation with labor, management, and senior advocacy organizations, could develop and conduct a public information and education campaign for workers and their families.

The National Committee to Preserve Social Security and Medicare does not recommend that all eligible individuals apply for Social Security benefits at the first opportunity. Quite the contrary, we believe many individuals would recognize their own self interest in delaying retirement in order to become eligible for higher benefits. The reason they do not do so now, is, first, the inadequacy of delayed retirement credits and, second, a lack of understanding of the economic consequences of retiring early versus deferring Social Security retirement.

Workers today do not understand the Social Security benefit structure or the way benefits are computed. They do not appreciate how many years of earnings are counted in computing benefits or if new earnings will make a difference. They do not know how or even if early or late retirement will affect their lifetime flow of benefits. Couples do not know that if a wage earner retires before age 65, survivor benefits will be based on the age the worker retired, rather than the age the spouse or widow begins receiving benefits. No wonder few can intelligently plan for the future!

The workers of this Nation can make sound judgments about their own future if they are given the facts. Unfortunately, most individuals receive their first, detailed information about actuarial reductions when they go to their Social Security Office to fill out an application for benefits. Even then, since the decision to retire already has been made, the claims representative does not discuss delayed retirement credits.

One component of the education campaign should be the perfection and widespread dissemination of the new Personal Earnings and Benefit Estimate Statements. This will help workers understand the difference in monthly benefits between retiring early and delaying retirement, and we commend the Social Security Administration for this initiative. But many workers will be misled because this information does not make it clear that spouse and widow benefits are totally offset by personal benefits. Nor are public employees cautioned that their benefit estimates are overstated.

The National Committee recommends that the Personal Earnings and Benefit Estimate Statement be modified to improve and expand the information provided, and that the Social Security Administration be required to periodically send an up-to-date statement to each and every worker. Receiving more and better information earlier will enable workers and their spouses and survivors to make intelligent and responsible retirement choices.

CONCLUSION

Economists deplore the trend toward earlier retirement and warn us that, as a nation, we cannot afford to continue losing the talents and energies of our older citizens. If we are serious about reversing this trend, one place to start is by removing disincentives in the Social Security program and, instead, replacing them with Social Security economic incentives for continuing in the work force. The National Committee's proposal for equitable delayed retirement credits for all individuals -- combined with total cancellation of the earnings limitation -- will satisfy these objectives. At a minimum, Congress should move forward with interim steps, such as increasing the earnings limit.

We thank you for this opportunity to present our views on eliminating the retirement test.

NATIONAL COMMITTEE TO PRESERVE
SOCIAL SECURITY AND MEDICARE

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SOCIAL SECURITY WORKING WIDOW EQUITY PROPOSAL

Proposals outlined below would provide widows an opportunity to increase Social Security widow benefits by continuing in the work force and would assure that all family members share in delayed retirement benefits.

1. **When workers retire early, reduce benefits to their widows only if the widows themselves will receive, or have received, early retirement benefits.**

2. **When widows remain in the work force past full retirement age, apply delayed retirement credits to widow benefits as well as to the widows' own Social Security benefits thus assuring that, upon retirement, widows will receive delayed retirement credits in return for benefits foregone.**

3. **When workers earn delayed retirement credits, add those credits to the primary insurance amount so family members eligible for benefits share in extra credits earned by extra years of work.**

Background:

Wage earners and spouses can apply for and receive early retirement benefits at age 62, widows at age 60. But in all instances, early retirement benefits are reduced to compensate for the long~~er time that~~ benefits will be paid. The maximum number of reduction months will rise as the full retirement age rises in the next century.

Wage earners who delay retiring, or who have some months of benefits offset due to earnings above the annual earnings limitation, receive a delayed retirement credit for months between ages 65 and 70 that retirement benefits are not paid. The current credit of three percent per year is scheduled to rise gradually between 1990 and 2008 to an actuarially equitable eight percent.

When workers retire before full retirement age, whether they live one month or 20 years after retirement, benefits to their widows are computed as if the widows retired at the age the deceased husbands retired. For example, if a worker retires at age 62, benefits to his widow are computed as if she retired at age 62, even if she continues working and never receives widow benefits before age 70.

Conversely, if workers retire at age 65 or later, benefits to their widows are reduced only if the widows themselves are less than 65 when they begin receiving widow benefits, even if they have previously received reduced spouse or worker benefits. If workers earned delayed retirement credits, their widows will receive those delayed retirement credits.

Technically, a widow who enters in or continues in the work force past age 65 receives her own delayed retirement credits for any month after age 65 that she does not receive Social Security benefits. If her own benefits are greater than her widow benefits, she will receive delayed retirement credits. But if her widow benefits are the greater amount, when she retires, she will actually receive no delayed retirement credits whatsoever. Any increase in her own benefits simply decreases the additional amount she is eligible to receive as widow benefits. The benefits paid will be identical to those she would have received if she had never entered the work force or had retired at an earlier age.

Equity demands that any delayed retirement credit percentage earned by widows who continue in the work force be added to the monthly benefits that would have been paid had the widows not been working.

Equity also demands that delayed retirement credits be added to benefits paid to dependent family members. At the present time, retired workers who have earned delayed retirement credits receive those credits in their own benefits. But benefits to spouses and dependent children are computed as if the worker had retired at age 65. This diminishes by at least half the value of delayed retirement credits to married retirees.

Social Security Administration actuaries have estimated the five year, 1990-1994, cost of proposal No. 1 at $690 million and proposal No. 2 at $175 million. No estimate has been made of proposal No. 3.

Working widow protection legislation has been introduced in prior Congresses. Revised bills will be reintroduced in the near future.

Chairman **Jacobs**. That is the end. Well, thee is right, friend, that is the end. This concludes the hearing and we thank this panel for its contributions to the record.

[Whereupon, at 12:55 p.m., the hearing was adjourned.]

[Submissions for the record follow:]

A STATEMENT ON THE RETIREMENT EARNINGS TEST

by

SENATOR WILLIAM L. ARMSTRONG

MR. CHAIRMAN:

Back in 1983 when the Social Security solvency amendments were considered, the Senate approved a proposal that would have phased out the Social Security Retirement Earnings Test. Although this provision was dropped in Conference, the earnings limit remains one of the most unpopular features of the Social Security program. Twenty-six bills (with 151 cosponsors) to modify substantially or eliminate the test were introduced in the 100th Congress and at least 12 bills have already been introduced in this 101st Congress. Clearly, the will of the people and the intent of the Congress is that some action be taken to right this injustice.

Here is how the earnings limit works now. Social Security beneficiaries under age 70 face sharp reductions in their monthly benefit if their wage earnings exceed a specified amount. These seniors will lose fully $1 of benefits for every $2 in earnings they receive above the limit, currently set at $8,880. Next year, the penalty for earnings above the limit is sceduled to "improve" to losing $1 in benefits for every $3 in earnings received above the limit of $9,360. This means that a senior worker who should be in the lowest tax bracket may end up paying effective marginal tax rates as high as 83% (50% earnings test, 15% income tax, 7.51% FICA, 7.5% income tax on Social Security benefits, and 3.37% Catastrophic). Those uncomfortable with the description of the earnings limit as a marginal tax rate, can simply consider it a "marginal disincentive to work" measurement.

Social Security was started in the wake of the Great Depression. At that time, it was deemed appropriate to establish incentives for the elderly to leave the work force to open jobs for others. Today, such a notion is a complete anachronism. When potential labor shortages loom in the future -- shortages that are already a reality in parts of western Europe -- it is utter folly to retain such a strong disincentive for America's elderly to continue working.

The earnings limit is bad labor policy, pure and simple. According to the Social Security Administration, 855,000 people currently have their benefits reduced because of the earnings cap. Caught in the retirement earnings test trap, many of our elderly have been driven out of the workforce altogether. Today, 83% of all men and 92% of all women age 65 and over are completely retired. Between 1970 and 1985, the retirement rate among those 65 years old has increased by 40%.

The earnings limit is bad social policy. As stated earlier, it imposes a strong disincentive on elderly citizens who want to continue working. After contributing to Social security for decades and reaching age 65, the elderly are presented with a painful choice: eliminate virtually all significant earnings or face stiff cuts in the benefits to which they are otherwise entitled. That kind of choice drives productive individuals to a full retirement or forces them to forego benefits they've worked for over a lifetime.

This line of thinking is not without some critics. Some may say that retirement benefits should not be paid to people who still work at all. Again, that view would either discourage senior citizens from pursuing productive lives, or deny them the benefits of a program to which they were forced to contribute during their decades of full-time work. Although the opposing argument is based on the tenet that benefits were to be paid upon retirement rather than attainment of the normal retirement age, it is woth noting that O.A.S.D.I. stands for **Old Age** Survivors and Disability Insurance. Of course, no one should feel comfortable in describing Social Security as an insurance program in the strict sense, anyway. After all, if it were an insurance program people could choose to not "buy the policy." Importantly, **no one has this**

choice. In fact, if someone who is 66 years old decides to take a part-time job at a local drug store, part of every paycheck still goes to Social Security.

Others complain that a liberalization or elimination of the earnings limit would simply benefit the wealthy. Addressing this charge necessitates focusing on the difference between "income" and "earnings." In reality, a person can have unlimited unearned income from pensions, investments, or stock dividends and face no reductions in benefits through the earnings test. At the same time, a retired school teacher who decides to substitute teach to supplement her benefits will lose 50 cents in benefits for every dollar that she earns. It is true that neither the super-rich nor the very poor will probably benefit from liberalization or elimination of the earnings limit. Instead, such action will help the low to middle income elderly.

For example, a 1988 working paper by the Congressional Budget Office asserts that "among those affected by the earnings test, most women, widows and widowers, and people with low family incomes would become exempt if the earnings limit were doubled." Just a $1,000 increase in the limit is estimated to make 85,000 currently earning between $9,000 and $10,000 a year completely exempt from the penalty. Virtually none of those affected by the limit are "wealthy." Rather, CBO data from 1986 reflects that nearly three-fourths of those affected had incomes between $21,000 (single) and $26,500 (couple).

Why is the earnings limit so unpopular both with the public and within Congress? Besides the basic inequity involved in punishing someone for continuing to contribute to society, I believe there is a general rebellion against the concept of Social Security as a welfare program for senior citizens. If our goal as a society is to have our elderly population truly existing at a poverty level, the surest way of ensuring that result is the perpetuation of the retirement earnings test. For if our elderly were actually expected to live on their Social Security benefit payments they would almost certainly fall under the poverty level. If, instead, Social Security is interpreted as a program designed to supplement the wellbeing of America's senior citizens and guarantee them a certain quality of life, elimination of the retirement earnings test is simply consistent with that philosophy. Social Security benefits are properly regarded as a floor, not a ceiling.

In his inaugural address, President Bush made a statement with which I believe most will agree. He stated, "We must bring in the generations, harnessing the unused talent of the elderly ..." The first step toward realizing this goal is phasing out the retirement earnings test.

Helen Delich Bentley
Member of Congress

COMMITTEE STATEMENT
BY THE
HONORABLE HELEN DELICH BENTLEY
FOR
THE SUBCOMMITTEE ON SOCIAL SECURITY
ON
REPEAL OF THE SOCIAL SECURITY EARNINGS TEST

May 25, 1989

Mr. Chairman:

I am particularly honored to be here today with several of my most esteemed colleagues. The opportunity to testify is certainly appreciated. Repeal of the earnings test has been tossed through the legislative cycle for many years--it is now apparent that a serious move towards repeal of the restrictions is underway.

At one time or another, opponents and proponents alike have vociferously pounded Congress with their arguments: Simply, the earnings test should be dropped because it prevents older Americans from working OR the earnings test should remain because removal only benefits high income older Americans.

However, at the time the earnings test was enacted, there was an abundance of younger workers entering the job market. The rationale was: "Out with the old and in with the young". And so we did.

Today, this picture is no longer accurate. In many fields, there are no young people waiting in line for an older worker to retire. In fact, a slew of corporations including Travelers, Bank of America, Wal-Mart, Ashland, Kodak, Polaroid, 3M and IBM, to name a .mt few, are involved in older worker retention programs. They want to keep their older workers!!

Corporations want to keep their older workers because they have institutional knowledge. In today's complex society, knowledge of origin and context are imperative to the smooth function of both government and the private sector. We really cannot afford to cloet all of this experience and knowledge if our nation is to be competitive with the rest of the world.

It is important to remember that repeal of the earnings test is not about making the wealthy elderly better off. It is about curbing the imminent labor shortage our country will be facing at the turn of the century.

Several Washington Post editorials have incorrectly asserted that older individuals do not care to work. I understand this sentiment, false as it is, because our society has been trained to think that older people are better off rocking and knitting. Although there are many prospective retirees who dislike their current occupations, upon retirement many seek another line of work. We are a society of workers--right or wrong, it is how we define ourselves.

The fact that so many of our retirees are giving extensive hours every week in volunteer tasks just to keep busy dispels the myth that older persons do not care to work. This is certainly true in my district where nearly 25% of the constituency is sixty years of age or older. Several stop me at least once a month to ask what is happening with the Social Security earnings level.

I agree that one intent of Social Security is to partially replace income lost at retirement. However, this reasoning does not solely include the earnings question. Rather, this argument points towards raising the retirement age above 65.

I have seen a need--as evidenced by the policies of the aforementioned companies--and a desire on the part of older Americans, to remain in the workforce at some capacity after age 65. As we enter the next century, older workers will become essential to the smooth operation of our industrial base and our service sector.

I agree with Congressman Archer's statement that allowing the older worker to be able to make a choice will have a positive effect on the medical needs of the elderly. Medicare costs will surely decrease.

As demographic trends continue to alter our perspective on retirement and social security, Congress should consider a redefinition of the earnings test. A repeal of the law may be a bit much, but altering the tax to one dollar for every three earned may be a prudent first step in the earnings test debate.

Why react to a future problem when we can proactively bring about change now? The earnings test should be modified.

Congressman
David Dreier

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Remarks of the Honorable David Dreier
Before the House Subcommittee on Social Security
May 25, 1989

Mr. Chairman, there are few issues that I feel as strongly about as the outside earnings limitation. Our policy is simply unfair and illogical anyway you look at it. Because I have been working for the elimination of this policy for a number of years, I have received scores of letters from senior citizens across the country who NEED to work - yet we slap a 50 percent tax on their earnings. Let me suggest that this is nonsensical. The Tax Reform Act was passed with the argument that lower income tax rates would increase work effort. The earnings test totally disregards this. In fact, some senior citizens will face 1989 marginal tax rates of over 100 percent when the earnings tax and the new Medicare Catastrophic Protection Act tax kick in. These citizens are in a higher tax bracket than any other wage earner.

The earnings limitation originated with every good intention. Social Security is a partial retirement program meant to cushion a senior's lost earnings. The earnings limitation encouraged senior workers to fully retire, thereby making room for younger workers at a time when job opportunities were scarce and 50 workers were supporting every beneficiary. I don't agree with this argument now any more than I would have then, but I'm sure we can all agree that things have changed dramatically since the Thirties. The Social Security program is still a partial retirement plan, yet one-quarter of all retired people depend on it for 90 percent of their income. Demographics have also changed - only three workers support each Social Security beneficiary now. The earnings test is outdated and in desperate need of revision.

The people most hurt by the Social Security earnings test are those who most need extra earnings -- those who have had a career of low earnings and who did not qualify for employer pensions. Those who earn huge incomes from private pensions or investments don't lose a dime in Social Security benefits. Yet, those who earn more than $8,880 a year answering phones do. Again, I suggest that the earnings test is nonsensical.

I don't believe that any American should be discouraged from working. The earnings limitation is one of the remaining - though indirect - mandatory retirement policies imposed by the federal government. And this policy affects a significant number of elderly. The Social Security Administration estimates that each year about 1.4 million beneficiaries lose some or all of their benefits as a result of the earnings test. These people paid into this system and deserve their benefits regardless of there employment status. The Social Security system is not a means-tested welfare system. No private retirement system would discourage its recipients from working at other jobs.

In addition to hurting senior citizens, the Social Security earnings test hurts today's workers by acting as a disincentive to planning ahead for the retirement years. What we say is: plan ahead; Social Security is a partial retirement plan. And yet our policy says the opposite. We must give today's workers the incentive to save, and repeal the disincentives to earn.

Eliminating the earnings test makes sense for senior citizens and for Social Security. It is difficult to estimate the cost in the short term, as it is uncertain how many elderly would return to the workforce, resulting in more revenues from federal income taxes, payroll taxes, and taxation of Social Security and Medicare benefits. But one thing is certain: elimination of the earnings test will not HURT the Trust Funds in the long- or short-term. Benefits will not be affected and the solvency of the Trust Funds will remain strong.

Mr. Chairman, in summary, I believe it is time the outside earnings limitation, not older workers, be retired. I have introduced legislation called the Retirement Equity Act that eliminates the outside earnings limitation, the tax on higher-income beneficiaries which was imposed in 1983, and the FICA and SECA tax on workers over age 70. I am hopeful that this bipartisan effort will encourage Congress to move forward on a change that is fair and makes good economic sense.

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